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Building a Smarter Planet: 1 in a Series

Welcome to the decade of smart.

A year ago, we began a global conversation about how our planet is becoming smarter.

We talked about intelligence being infused into the systems and processes that make the world work—into things no one would recognize as computers: cars, appliances, roadways, power grids, clothes, even natural systems such as agriculture and waterways.

We said that trillions of digital devices, connected through the Internet, were producing a vast ocean of data. And all of that information—from the flow of markets to the pulse of societies—could be turned into knowledge because we had the computational power and advanced analytics to make sense of it all.

A year into this new era, the signs of a smarter planet are all around us. Smarter systems are being implemented and are creating value in every major industry and across every region of both the developed and developing worlds.

This idea isn't a metaphor, or a vision, or a proposal—it's a rapidly emerging reality.

In a study of 439 cities, those with transportation congestion systems showed an average reduction in travel delays of more than 700,000 hours annually.

A yearlong study by the U.S. Department of Energy's Pacific Northwest National Laboratory found that consumers within smart meter systems saved 10% on their power bills and cut their power usage by 15% during peak hours.

Eight hospitals and 470 primary care clinics were able to improve clinical results and operational efficiency by up to 10% through information access at the point of care.

Leading retailers have reduced supply chain costs by up to 30% and increased sales by up to 10%—through analyzing buying behaviors, aligning merchandising with demand and building end-to-end visibility from manufacture to sale.

Everywhere, forward-thinking leaders are achieving near-term ROI. But they are also discovering something deeper. They are finding the hidden treasures buried in their *data*.

Data is being captured today as never before. It's revealing everything from large and systemic patterns—of global markets, workflows, national infrastructures and natural systems—to the location, temperature, security and condition of every item in a global supply chain.

Then there's the growing torrent of information from billions of individuals using social media. They are customers, citizens, students and patients. They are telling us what they think, what they like and want, and what they're witnessing. In real time.

That's a lot of data, but data by itself isn't useful. In fact, it can be overwhelming—unless you can extract value from it. And now we can. With the right tools, we are beginning to see patterns, correlations and outliers.

With sophisticated mathematical models, we can take the measure of the world's information and actually begin to predict and react to changes in our systems. New York has smart crime fighting. Paris has smart healthcare. Galway has smart water. A smart grid in Copenhagen keeps energy flowing.

We've learned a lot over the past year about what it takes to build a smarter planet—and about the issues it raises. Issues like protecting personal information and securing critical infrastructures. We've learned that we will need global standards across all dimensions of these complex systems. New skills and fields of expertise. New ways of working and thinking. A smarter planet also requires a profound shift in management and governance.

Business leaders, policymakers and government officials around the world understand these challenges, and are stepping up to them. Above all, they realize that we cannot wait, cannot let this moment pass. The time to act is now. And the way to act is together. The decade of smart is under way.

Let's build a smarter planet. Join us and see what others are doing at **ibm.com/smarterplanet**

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Bloomberg BusinessWeek In Depth

32 | Obama's Corporate Messaging

In a wide-ranging Oval Office interview, President Barack Obama takes aim at the perception that he and his Administration are anti-business

38 | Detroit's Big Chance

GM and Ford have a rare opportunity to steal buyers from a bloodied Toyota. The trick is not to seem predatory

46 | Caribbean Tax Holiday

The IRS is investigating how $100 billion a year in retail credit-card receipts is escaping U.S. taxation

50 | Goodbye, Ireland

With the day of the Celtic Tiger now a memory, a job famine is forcing a new generation to head overseas

54 | Memo to Lloyd Blankfein

Michael Lewis on how to make mere mortal Americans more properly appreciative of Goldman Sachs



(COVER CREDIT) MARCO GROB; (THIS PAGE) PHOTO ILLUSTRATION BY DAVID RUDES/BW; PHOTOGRAPH BY KIMBALL STOCK COLLECTION

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BusinessWeek The Global Report



A demonstrator in central Athens

The Week in Business

08 | Executive Summary Bernanke on interest rates; a peek at China's wealth; shakeup at SAP

14 | At the Table Charlie Rose talks with billionaire Eike Batista about the oil boom ahead in Brazil

16 | Business Outlook Why small business isn't leading the recovery

17 | Numbers A wide world of crushing government debt

New Business

18 | Greek Ruins Bond market vigilantes are making Athens pay for failing to lower deficits

22 | BW 50 Google on Display For the search-ad king, display advertising will soon be a billion-dollar business

24 | Inside the iPad Apple's new tablet is more than the sum of its parts—about $270 more

26 | No Rest for UBS The Swiss bank is profitable again, but CEO Oswald Grübel still needs to stem the exodus of wealthy clients

29 | Buying Opportunity With health-care reform on hold, hospitals and insurers are looking to consolidate further

30 | Less Yummy in China What's behind slowing sales at Yum! Brands' KFC and Pizza Hut

What's Next

64 | Let's Make a Deal After years spent stabilizing Tyco, CEO Ed Breen sees acquisition as the company's key to growth—again

66 | Chutes and Ladders Electronic Arts tries to climb out of a deep hole as game players turn to cheaper online alternatives

67 | Hedge Row The financial industry and EU regulators spar over proposed rules for hedge funds

68 | The Street's Bête Noire CFTC chief Gensler, a Goldman vet, emerges as a tough regulator

70 | Judgment Day Care A new service minds pets "left behind"

71 | Global Designs Tory Burch takes on the world

72 | Golden Board Pay is soaring for big-time corporate directors. And so is the workload

Personal Business

74 | Money Report How Fibonacci might predict the market; Wells Fargo braces for higher interest rates; the Fed's happy returns

75 | Tops in Tough Times Mutual funds that rode both the bear and bull in 2008 and 2009

76 | Second Acts A retired banker teaches nonprofits how to raise money the way Wall Street does



Burch has proved she's no dilettante



Palm's Pre Plus: Bring the Wi-Fi with you

Business Views

78 | Books Gawande: *The Checklist Manifesto: How to Get Things Right*

80 | Tech & You Rich Jaraslovsky, a walking mobile hot spot

81 | Feedback AT&T's iMess

84 | Outside Shot The surprising effectiveness of straight talk

81 | Corrections & Clarifications

82 | Company Index

(TOP) SIMELA PANTZARTZI/EPA/CORBIS; (CENTER) DANIEL ACKER/BLOOMBERG

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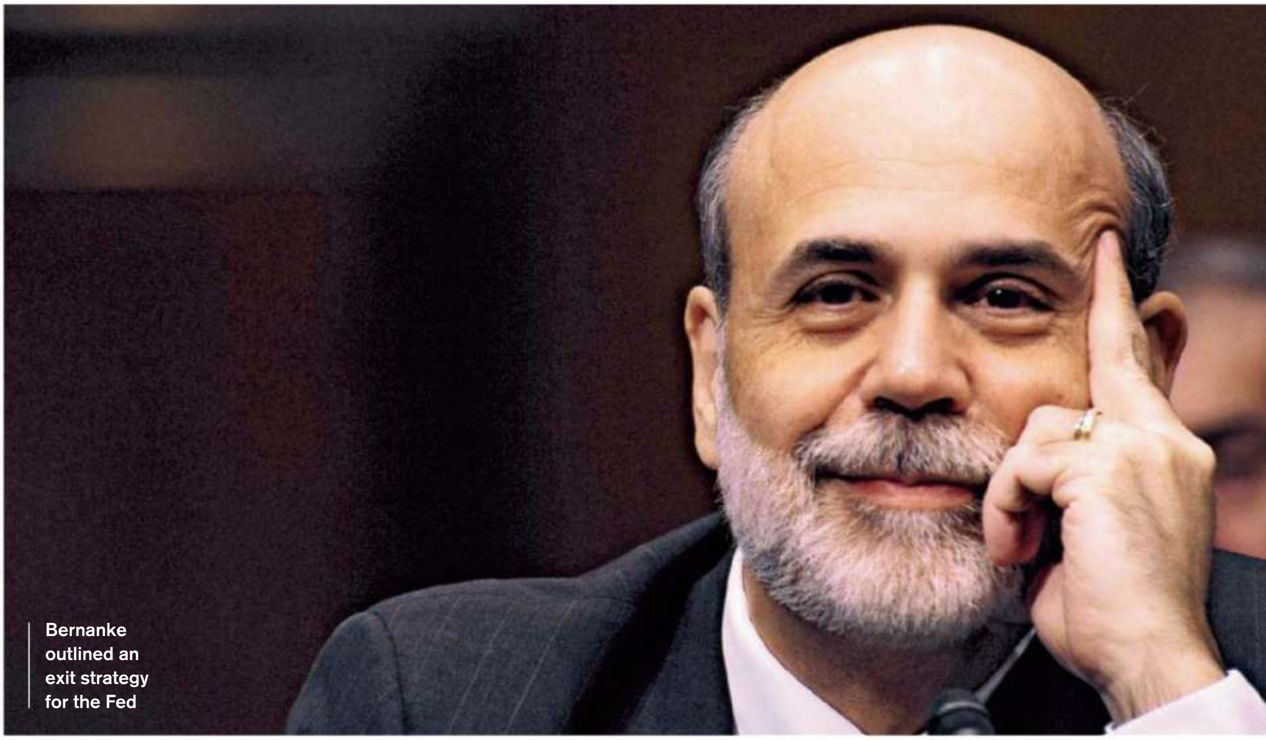
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THE WEEK IN BUSINESS

Edited by
Cristina Lindblad



Bernanke outlined an exit strategy for the Fed

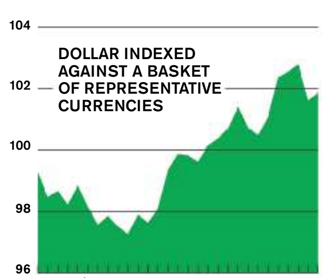
ECONOMICS & POLICY

THE FED'S NEW TOOLBOX

Neither snow, nor sleet—nor a whole lot of snow and sleet—could keep **Ben Bernanke** from laying out the mechanics of the Fed's plan to wean the U.S. economy from stimulus. With his Feb. 10 hearing before Congress canceled because of a winter storm, the central bank chief posted his prepared remarks on the Fed's Web site. Bernanke raised the possibility that the Fed might shift from using the federal funds rate—the rate banks charge each other for overnight borrowing—as its primary tool in monetary management. Instead, it would target the interest rate payable on deposits institutions hold in reserve with the central bank. By boosting the rate on reserves, banks would have more incentive to stash money at the Fed, a move that Bernanke said would, "put significant upward pressure on all short-term interest rates." He refrained, however, from setting a timetable for tightening.

DOLLAR BOOST

Economic weakness in Europe has bouyed the greenback



Data: Bloomberg

AVERTING A GREEK TRAGEDY

Markets around the globe seesawed as investors took bets on whether the wealthier nations of Europe would come to the aid of their poorer relations. Facing the possibility that a debt default by Greece might drag down the euro, European leaders initially stood firm, saying Athens could get its act together on its own through spending cuts and tax hikes. But by Feb. 10, Germany was moving toward granting some kind of assistance—with stringent conditions. Prices of Greek, Portuguese, Spanish, and Irish bonds rose on the news.

| BW | PAGE 18 "The Bond Vigilantes Who Left Greece in Ruins"

WEALTH OF NATIONS

Bowing to calls for greater transparency, China's $300 bil-

11%

Decline in U.S. corporate bond sales so far this year from the same period in 2009

Data: Bloomberg

KAREN BLEIER/AFP/GETTY IMAGES; CHART BY DAVID FOSTER/BW

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EXECUTIVE SUMMARY

lion sovereign wealth fund for the first time filed a quarterly report with the **U.S. Securities & Exchange Commission** detailing its U.S. holdings. The filing by **China Investment Corp.** for the period ended Dec. 31 reveals a move away from bets on individual stocks and toward commodity and sector funds. Such exchange-traded funds made up about 25% of the $9.63 billion in U.S. equity holdings reported by the Chinese. CIC, which was created in 2007, initially plowed billions into stakes in Wall Street firms **Morgan Stanley** and **Blackstone Group,** only to see the value of those holdings slump in the wake of the financial crisis.



CIC Chairman Lou Jiwei is steering clear of big U.S. equity investments

LEADERSHIP

SHAKEUP AT SAP

Auf wiedersehen, Leo. **Leo Apotheker,** CEO of **SAP**, the German company that is the world's top maker of business management software, tendered his resignation on Feb. 7 after the board declined to extend his contract. In his nine months at the helm, Apotheker presided over the first major layoffs in the company's 38-year history and an 4% slide in profits in 2009. He will be succeeded by board member **Bill McDermott** and product development chief **Jim Hagemann Snabe**. The co-CEOs have difficult work ahead. Management acknowledges that customers are restive and employee morale is sagging. Also, SAP has been slow to adapt its software for the Web and mobile devices.

"What SAP Needs After Apotheker"
businessweek.com/magazine



Thain has been tapped to lead commercial lender CIT

THAIN'S NEXT ACT

Lehman Brothers' Dick Fuld and **Bear Stearns's Jimmy Cayne** may be laying low, but another unemployed Wall Street banker has returned to a corner office. On Feb. 8, **John Thain**—former CEO of **Merrill Lynch** and the **New York Stock Exchange**—was named to lead **CIT Group**, the commercial lender that emerged from bankruptcy in December. Under another Merrill man, former CEO **Jeffrey Peek**, CIT embarked on a disastrous foray into subprime lending. Thain must now steer the crippled firm, which makes loans primarily to small and medium-sized companies, back to health or into the arms of a buyer. He will receive an annual salary of $500,000, plus $5.5 million in shares.

STRATEGY

TOYOTA IN A TAILSPIN

Toyota Motor's reputation for quality and reliability suffered further damage on Feb. 9 when the Japanese automaker announced the recall of 437,000 cars, including its flagship Prius, to fix a brake problem. The

THE OPTIMISM METER

SEVEN-MONTH LOW



The Meter clocked in at 31 on Feb. 9, down from 45 the week before and the lowest reading since last July. Amid elevated stock market volatility, the share of Americans who believe the market will be lower 12 months from now rose by 22% from the prior week. Developed by ***Bloomberg BusinessWeek*** using data from pollster **YouGov**, the Meter is a proprietary measure of sentiment and expectations, economic statistics, and market forecasts. It evaluates shifts in outlook among individuals, professional investors, and economists in the areas of U.S. economic growth, jobs, equity markets, and real estate.

Calculated using consumer polling, economic forecasts, and financial markets data; 0=lowest and 100=highest Data: YouGov, *Bloomberg BusinessWeek*

(FROM TOP) MARK WILSON/GETTY IMAGES; NELSON CHING/BLOOMBERG NEWS

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EXECUTIVE SUMMARY

move follows the recall of nearly 8 million Toyota vehicles globally because of problems linked to unintended acceleration. Congress plans to hold hearings to determine whether Toyota and the **U.S. National Highway Traffic Safety Administration** initially ignored consumer complaints about sticky gas pedals.

| BW | PAGE 38 "Detroit's Big Chance"

ASIA-LED RECOVERY

Americans have tightened their belts, but folks elsewhere continue to eat and drink merrily—good news for the likes of **McDonald's** and **Coca-Cola**. On Feb. 9 the companies reported that while sales fell in North America during the most recent period, overall revenue was up, thanks to higher sales abroad. Reporting a 4% rise in operating income for the fourth quarter, Coke noted that it sold 1% fewer cases of soft drinks in the U.S. and Canada but 29% more in China. At McDonald's, January same-store sales slipped 0.7% in the U.S., but increased 4.3% in Europe and Asia/Pacific.



China lifts Coke's worldwide sales

TECHNOLOGY

FEEL THE BUZZ

Confronted with the rapid rise of **Facebook** and **Twitter**, **Google** is taking another shot at owning a piece of the social Web. On Feb. 9, Google unveiled **Buzz,** a service for sharing short messages, images, videos, and links. While critics say Buzz merely duplicates many of the functions already available to Facebook's more than 400 million users, Google says its service will help users find the messages and multimedia most interesting and relevant to them. Also, in a direct challenge to phone companies, Google announced plans on Feb. 10 to test a high-speed broadband network to serve as many as 500,000 people.

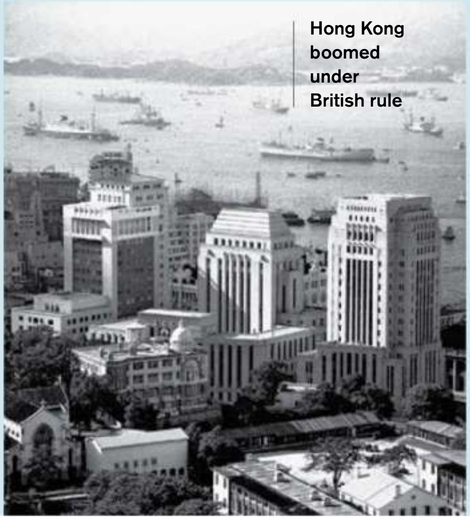
| BW | PAGE 22 "Google's New Billion-Dollar Baby"

"Google Buzz Won't Weaken Facebook" businessweek.com/magazine

IDEAS CHARTER CITIES

Disasters such as the earthquake in Haiti are capable of mobilizing a global community of aid donors. But relief efforts, no matter how well funded, are rarely enough to set impoverished countries on a path to prosperity.

To do that, policymakers must devise ways to unlock the entrepreneurial drive of the poor. That goal could be accomplished through the creation of charter cities, argues **Paul Romer** in an article in the January issue of *Prospect,* a British magazine. Romer, a development expert affiliated with **Stanford University**, envisions an arrangement between poor and developed countries under which the former cedes a patch of land and the latter is responsible for writing and enforcing the laws that govern commercial and other activities within the territory. There are precedents for such partnerships. Hong Kong flourished under British rule, and the island nation of Mauritius, where the British privy council is still the court of final appeal, boasts one of the highest standards of living in sub-Saharan Africa. "The credibility of rules developed over centuries by the British government was essential to attracting foreign investment, companies, and skilled workers" to Hong Kong, says Romer.



Hong Kong boomed under British rule

But there have also been failures. In the 1990s, Singapore tried to establish variants of charter cities in China and Indonesia but ran into dificulties because local authorities retained too many discretionary powers.

Romer's is a provocative idea—one that smacks of neocolonialism. Radical solutions may be needed, though, to pull countries like Haiti, which has defied conventional approaches, out of a downward spiral.

Prospect "For Richer, For Poorer"

(FROM TOP) TENGKU BAHAR/AFP/GETTY; AP PHOTO

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Smarter business for a Smarter Planet:

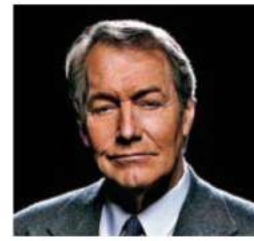
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A smarter business needs smarter software, systems and services.
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"We believe that in five years Brazil will be the fifth-largest economy in the world"

EIKE BATISTA
Rich Man. Richest Man?

Eike Batista—known as a swashbuckling businessman and no stranger to the gossip columns—is already said to be the wealthiest person in Brazil. Because of his oil holdings and interests in a vast number of other businesses, he may well become the richest man in the world. Batista, one of seven children of a high-level government official, got into gold at an early age and eventually controlled mines from Chile to Russia. In addition, he has been involved in energy, water, and steel companies. Now Batista is betting that Brazil will be a major oil power.

CHARLIE ROSE
Fifteen years from now, what do you want to have achieved?

EIKE BATISTA
We believe that in five years Brazil will be the fifth-largest economy in the world. And we're just one of the many companies helping Brazil grow. Obviously, the oil discoveries will [bring about enormous changes]. We're talking about 100 billion barrels of recoverable oil.

Your father is a very distinguished Brazilian.
What I learned from my father is to think big. There's a movie called *Brazil's Engineer*, and it's about him because he built part of [the country's] infrastructure—railways, super ports to ship iron ore to Asia. But I was educated by my mother because my father was very busy. She was German, from Hamburg, and she taught me discipline and caring for others.

(TOP TO BOTTOM) BRAD TRENT; PAULO FRIDMAN/CORBIS

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You were educated in Germany?
Basically, up to my 12th year, I was educated in Brazil. Then I lived in Europe, following my father, who was internationalizing CVRD [Companhia Vale do Rio Doce, now Vale, one of the largest mining companies in the world].

At age 23 you went back to Brazil and started out with a gold mine on the Amazon.
Initially, I started a trading company to buy the gold and sell it. After a year and a half, there I was at 23 with $6 million in my hand. And margins were going down because competition started to come in. I said, "I have to reinvent myself. Why not buy one of these rich pick-and-shovel mines and mechanize it?" By 1983, I had Brazil's first alluvial mechanized gold mine running in the Amazon jungle. I underestimated the weather, technical conditions, diseases, logistics—but ultimately the mine was so rich, it was idiot-proof because it survived all my mistakes.

So the moral is, if you're going to take a risk, make sure the payoff at the end is enough to justify the problems. Was the principle the same when you bid for the oil exploration sites off the coast of Brazil and took great risks?
The same principle. But you know, over time you learn that knowledge is important. So I hired a team of executives from [the Brazilian state oil company] Petrobras who had great knowledge. Finding oil is a multidisciplinary science. You need a lot of people—statisticians, engineers, and geologists, of course. And what I have learned in the past 30 years is that I read people better than I read books. So they showed me I could have a 60% success ratio: If I spend $1 billion dollars, at least $600 million would potentially find wealth. What I did was put up $1.3 billion to participate in the auction and... as of today, we have had 100% success. Every well we drilled since last August was a hit. Brazil will be producing 5 million or 6 million barrels of oil a day.

There was a period in your life when you were a speedboat racer. What was that about?

CHINA HAS ENDLESS DEMAND FOR OIL, FOOD, AND IRON ORE. MOST THINGS THEY NEED WE HAVE IN ABUNDANCE

I wanted an international title, and realized I couldn't outrun Ben Johnson in the 100 meters, so I said let me put some engines behind me. I won the Brazilian championship, then the world championship and the American championship. I got all the titles I wanted and got out. I didn't want to die, and my oldest son was born. You change your risk profile.

Do a bit of psychology for me. You had a famous father, you were married to a well-known woman—a former *Playboy* cover model. Was there a bit of you that said, "I have to find a way to make my mark, and I am going to become Brazil's richest man"?
Yes, it's part of the psychology, no doubt. I was educated to think maybe Brazil works, maybe it doesn't. But I decided I am going to make this country work for my children. I am investing all my effort now in making Brazil a great country.

What could your net worth be in the next 10 years?
$100 billion. But what is important is that Brazil is the highway for that. Did you know China has already surpassed the U.S. as our largest trading partner? China has endless demand for oil, food, and iron ore. Most things the Chinese need we have in abundance and can export. In 800 A.D., the Chinese had half of the world's GDP. In the next 20 or 30 years, I think they're back to 50% of the world's GDP.

In this new world economic order, what is the future of the U.S.?
From the outside, I see political gridlock. You have to start thinking out of the box. I believe in democracy, but let me tell you something that few people realize: In Brazil, our president can implement emergency measures for six months. That's exactly what he did when the world got into trouble in 2008, and that's why Brazil came out [of the financial crisis] so much faster than everybody else.

When you look at America, what concerns you, what encourages you?
You are now heavily indebted like Brazil was before. You have to be a little bit more Spartan. In the last 20 years you have focused too much on banking and finance. The best students went to banks or law firms. Where are the engineers? Americans should be driving electric cars, and you're not. | BW |


An offshore oil rig under construction near Rio in 2008

RENZO GOSTOLI/BLOOMBERG NEWS

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BUSINESS OUTLOOK | MICHAEL McKEE

IN THIS RECOVERY, SMALL BUSINESS FALLS BEHIND

The tiniest companies historically take the lead in economic rebounds. Not this time. Because of tight credit and frugal consumers, the little fish trail their larger brethren

Could small businesses become the Achilles' heel of the U.S. recovery? Companies with fewer than 500 employees helped lead the economy out of the last four recessions as entrepreneurs, sensing opportunity, opened new businesses. And smaller suppliers provided the tools and equipment needed for larger companies to boost production. But this time, almost six months after the U.S. economy began growing again, small businesses continue to cut capital spending and dismiss workers.

Such caution has big implications for the speed and strength of the recovery. That's because tiny businesses have an outsize impact on employment. In fact, total U.S. payrolls would have fallen between 1980 and 2005 without the jobs created by business startups—most of them companies with fewer than four workers, according to new U.S. Census Bureau data.

3%

Annual rate of job growth by small startups. It far exceeds the nation's 1.8% net job growth rate.

Data: U.S. Census Bureau

So a drop in the unemployment rate, which fell to 9.7% in January from 10% in December, may stall later this year if these companies don't start hiring. And growth likely won't meet the median 3% annual rate forecast for 2010 by 68 economists surveyed by Bloomberg without more small company investment.

"Will you have a sustainable recovery a few years down the road without getting some small business spending? No," says Cary Leahey, senior managing director at Decision Economics.

The U.S. economy expanded at a 5.7% annual rate in the fourth quarter, the fastest pace in six years. That surge was buoyed in large part by capital expenditures for equipment and software by large companies. But capital spending by smaller businesses remains depressed. Only 20% plan to spend money on equipment or facilities in the next three months, near a 35-year low, according to a survey released Feb. 9 by the National Federation of Independent Business. That could hurt the economy later this year, when big increases by large corporations are expected to slow as government stimulus money runs out.

Recent numbers suggest "the official data are too heavily weighted towards bigger companies, which are doing better than credit-constrained smaller firms," says Ian Shepherdson, chief U.S. economist at High Frequency Economics. However, he adds, "The latter employ half the workforce."

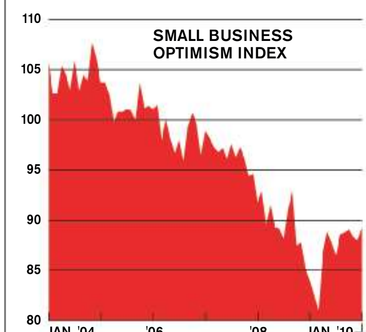
Surveys of small business owner sentiment don't presage a pickup anytime soon. The NFIB's index of small business optimism has been near historic lows for 16 consecutive months, hitting 89.3 in January. During the four prior recessions, going back to 1980, it dipped below 90 only once. Just 17% of NFIB members reported sales growth in the fourth quarter, while 47% saw declines. And just 1% said they expected conditions to be better in six months. "Optimism has clearly stalled, in spite of the improvements in the economy," says William Dunkelberg, the NFIB's chief economist.

Small companies have been particularly reluctant to invest in the one area the economy needs most right now: jobs. In January, small companies eliminated 3,000 jobs, according to Automatic Data Processing, the world's largest payroll processor. And in January, 19% of NFIB members reduced employment, while only 9% added workers. "They're still apprehensive about hiring people, because they're not seeing enough customers to translate into another worker," says Holly Wade, policy analyst at the NFIB.

Lack of access to credit also affects small businesses disproportionately. The Federal Reserve reported on Feb. 1 that banks were continuing to tighten standards for loans to small businesses, while standards for large companies were unchanged.

So far, there are few signs of improvement. PayNet's Small Business Lending Index, which tracks loans of $1 million or less, was 8.6% lower in December than a year ago. Although that's less than half the level of monthly decreases in early 2009, demand for expansion loans for small businesses is still 35% below its peak in 2006. Says PayNet President William Phelan: "That's another indication of how far we have to go to climb out of this recession." | BW |

SMALL COMPANY CONFIDENCE REMAINS IN A FUNK



Data: National Federation of Independent Business

CHART BY DAVID FOSTER/BW

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NUMBERS

A WIDE WORLD OF CRUSHING DEBT

By Tara Kalwarski/Charts by David Foster

National governments have nearly $55 trillion in debt—more than double the tally 10 years ago. Many countries, including Britain and Greece, may soon be downgraded.

Bond Boom Lower-rated countries have had the biggest percentage increases in government debt over the past 10 years.

GENERAL GOVERNMENT DEBT IN 2009*

RATING	BILLIONS OF U.S. DOLLARS	PERCENTAGE CHANGE SINCE 1999
Aaa	$33,444	125%
Aa	$14,874	93%
A	$2,140	204%
Baa	$2,835	297%

Data: Moody's Investors Service

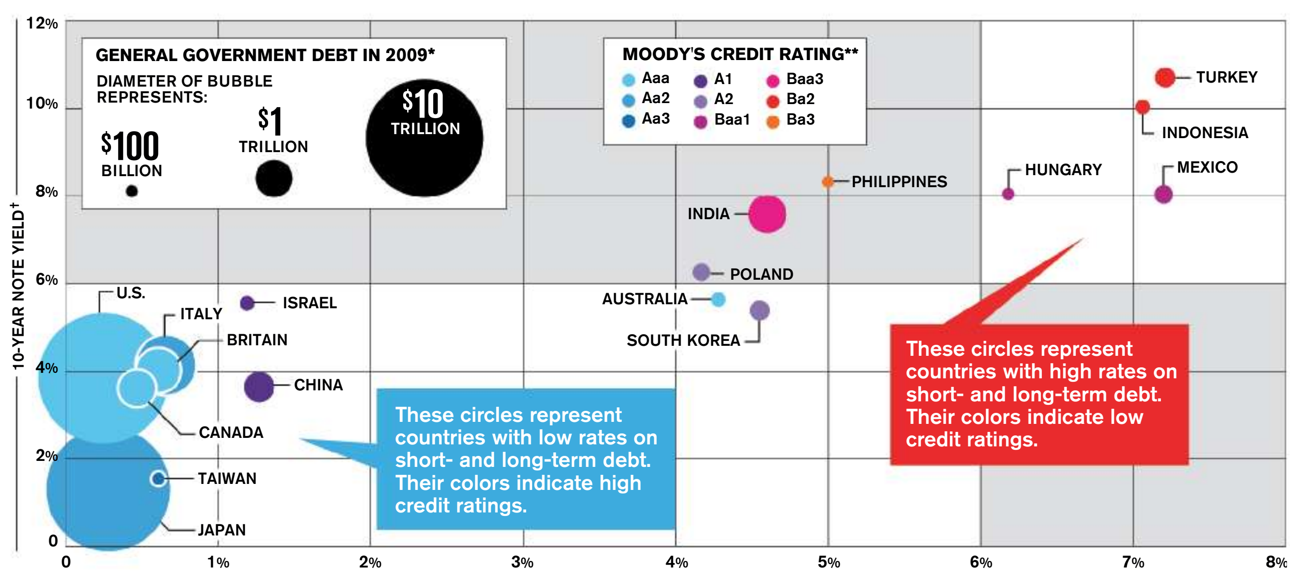
*Estimated in Nov. 2009

Credit Watch: Standard & Poor's anticipates lowering the ratings of these countries within the next 24 months.

COUNTRY	CURRENT RATING
Botswana	A
Britain	AAA
Estonia	A-
Ghana	B+
Greece	BBB+
India	BBB-
Ireland	AA
Japan	AA
Lithuania	BBB
Portugal	A+
Romania	BB+
South Africa	BBB+
Spain	AA+
Thailand	BBB+
Vietnam	BB

GOVERNMENT BORROWING: A GROWING BUBBLE

The U.S. and Japan are the world's biggest debtors, yet yields on their short-term debt remain extremely low. Higher yields reflect stronger growth prospects—as well as inflation and default fears.



Data: Bloomberg, Moody's Investors Service

*Estimated in Nov. 2009 **As of Jan. 26, 2010 †As of Q4 2009

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22 Google's new ad game
24 The iPad's guts
26 No rest for UBS
29 Health reform is dead. Let's go shopping
30 Is China fed up with the Colonel's chicken?

The Bond Vigilantes Who Left Greece in Ruins

Now, Europe is under pressure to rescue the Greeks while keeping other EU members in line

By Peter Coy

The European Union's experiment with a single currency is deep in crisis because Europe failed to learn from the Greeks. Not today's Greeks—the ancient Greeks, specifically Odysseus, the hero of Homer's epic poem. Odysseus knew his limitations. Realizing he was vulnerable to temptation, he ordered his sailors to tie him to the mast of his ship. That way he could listen to the bewitching song of the Sirens without obeying their call to steer the ship onto the rocks.

Today's Sirens are the investors and traders of the global bond market, who lure nations into tapping abundant credit at low rates when times are good. If a nation borrows too much, those open-handed investors abruptly turn into vigilantes who punish the country by making new loans scarce and expensive. Greece has fallen into precisely that trap. It got low-interest loans by promising to behave responsibly and keep its budget deficit low. That gained it admission to the single-currency zone in 2001. But because Greece was never tied to the mast, it kept spending. Its debt is now about 125% of gross domestic product, more than double the supposed EU ceiling. Eventually, all that debt brought down the wrath of the bond-market vigilantes, who drove up yields by betting against Greek debt, precipitating what has become the worst mess for the euro since the single currency's launch on Jan. 1, 1999.

At this point, Greece and the European Union have no good choices left. It's hard to see how Greece can muddle through on its own. On Feb. 10, striking labor unions shut down schools, hospitals, and air travel in a challenge to Prime Minister George Papandreou's austerity plan, which is intended to win back investors' confidence. Yiannis Kelekis, 68, a retired construction worker who joined a demonstration in rainy Athens, complained: "The people that caused the crisis are now asking for others to make sacrifices."

Noting the range of opposition, investors have concluded that Greece needs outside assistance to avoid default. If the European Union refuses aid, the government could find itself unable to issue $26 billion worth of debt as scheduled this spring. A Greek default—still considered highly unlikely—might trigger a run on the debt of Portugal and Spain. Like Greece, they belong to the PIGS—a name coined to describe Portugal, Ireland (and sometimes Italy), Greece, and Spain as the financial weaklings of Europe. "If Greece were alone in this, then possibly they would have been kicked out of the euro zone," says Diego Iscaro, economist at IHS Global Insight in London. "But they can't do that, because Greece is not alone." Stephen L. Jen, portfolio manager of BlueGold Capital Management, a London-based hedge fund manager, says German banks' exposure to debt of the five PIGS equals 19% of German GDP.

> "IF GREECE WERE ALONE IN THIS, THEN POSSIBLY THEY WOULD HAVE BEEN KICKED OUT OF THE EURO ZONE"

Trouble is, extending aid isn't a great choice, either. If the European Union helps Greece, then Portugal and Spain, whose finances are only slightly stronger, could demand similar help. That would stir resentment in the richer nations such as Germany and France. Worse, it would undercut the EU's

ILLUSTRATION BY DAVID RUDES/BW, PHOTOS BY LOUIE PSIHOYOS/SCIENCE FACTION/CORBIS; GREGOR SCHUSTER/CORBIS; AL ROD/CORBIS

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credibility as an enforcer of fiscal rigor.

As of Feb. 10, European officials seemed to be angling for a compromise plan to aid Greece but on such harsh terms that no one else would want such a deal. Germany and France were leading talks to help Greece under "tough preconditions," said Markus Ferber, a member of German Chancellor Angela Merkel's bloc in the European Parliament, citing discussions his group had with the federal officials in Berlin.

While Greece is uniquely dysfunctional, there's a lesson here for any country with a heavy debt load, including Britain, Japan, and the U.S.: The bond market is treacherous. For now, investors are pouring money into the U.S. Treasury market as a safe refuge. But the U.S.'s ratio of total debt to GDP is likely to exceed 90% this year, making it more indebted even than Spain and Portugal. If global investors began to demand higher yields to compensate them for the risk of a U.S. default, that would vastly increase U.S. borrowing costs. Higher debt service would worsen the nation's budget imbalance and possibly precipitate the very crisis that investors fear most. A long shot, to be sure, but not impossible.

Bond market speculators thrive in murky situations like this, where no one is ever quite sure what's true and what's a bluff. When Greece joined the euro zone, its borrowing costs fell to near-German levels because bond investors bought into the theory that Greece had finally become fiscally



An angry nation: Firefighters in Athens protest planned budget cuts ...

responsible. Lately, though, as Greece's fiscal weaknesses became clear, the profits have gone to those players who bet against Greek debt, shorting the bonds and talking up the bad news coming out of Athens. In the month through Feb. 10, the yield on the Greek government's three-month bills soared from less than 1% to 4%, raising the nation's borrowing costs.

Modern Greeks haven't had an easy time living up to their ancestors, who gave the world democracy, drama, and philosophy. According to economists Kenneth S. Rogoff of Harvard University and Carmen M. Reinhart of the University of Maryland, Greece has been in default for half of the time since it won independence from the Ottoman Empire in 1829.

Protests and strikes occur frequently in Greece because they tend to be profitable. "Every time somebody had to be bought off, they were bought off very generously," says Yale University political scientist Stathis N. Kalyvas. Meanwhile, Greece, like other small members of the European Union, has received extensive assistance from EU coffers. "The lesson being learned was not only was there no price to pay for not disciplining yourself, but in fact there was a benefit," says Kalyvas.

Greece seemed to be getting its act together a decade ago, when it was one of the fastest-growing economies in the EU. It reined in spending, reduced inflation, and cut interest rates. And it surprised critics by putting on a successful Summer Olympics in 2004. That proved to be the high point. Just after the Olympics, Greece acknowledged that it had understated its budget deficits for 2000, 2001, and 2002, meaning its fiscal gap had regularly exceeded the European Union's criteria for euro zone membership.

DEFAULT INSURANCE GETS COSTLIER

Prices of credit default swaps on sovereign debt have risen this year, indicating investors' greater nervousness that national governments will default on their debts. The prices represent the annual cost of insuring for five years against the default of government bonds with a face value of 10 million euros.



Data: CMA DataVision, Bloomberg

(L TO R) PHOTOGRAPHS BY PETROS GIANNAKOURIS/AP PHOTO; YIORGOS KARAHALIS/REUTERS; SIMELA PANTZARTZI/EPA/CORBIS

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... disgruntled farmers block highway traffic with their tractors ...



... and Greeks march in central Athens during a public-sector strike

Deficits continued. Last October the newly elected socialist government announced that the deficit was far worse than the previous conservative government had let on. That led to downgrades by credit-rating agencies, sparking the current crisis.

For now, the Greek government is still saying it can muddle through on its own. Greek Finance Minister George Papaconstantinou told Bloomberg Television on Feb. 8 that "the worst possible signal which we could send out is one calling for outside help."

Some economists see hope. Despite the unions' opposition, recent polls by Greek newspapers showed solid majorities backing the socialist government's austerity plan of spending cuts and tax increases. The vicious reaction of the bond-market vigilantes apparently convinced many Greeks that continued overspending was the road to ruin, says economist Elias Papaioannou of Dartmouth College. "People now have truly digested how serious and alarming the situation is," says Papaioannou. Adds Panagis A. Vourloumis, chairman of the Greek phone company Hellenic Telecommunications Organization: "This crisis could be a be a blessing in disguise if the government can push through the reforms that have been overdue for the last 30 years."

Investors, though, are dubious. That's evident from trading in credit default swaps on Greek debt, which pay buyers the full face value of a bond in case of a default. On Feb. 10 the price of default insurance was 356,000 euros per year for five years of protection on 10 million euros worth of debt, down 16% from two days earlier but still almost quadruple the price of last summer. Investors are skeptical that Greece will meet its goal of slashing its budget deficit as a share of GDP from 12.7% in 2009 to under 3% in 2012.

Greece and the EU wouldn't be in this no-win situation if they had followed their own rules from the start. But coming up with a mechanism that forces sovereign nations to do what's right when they feel like cheating is pretty much impossible. The EU has the authority to fine Greece as much as 0.5% of GDP every year until its shortfall is back in line, but that would just make the deficit bigger.

Americans can relate to the European dilemma. Congress had a pay-as-you-go budgetary rule in effect from fiscal 1991 through fiscal 2002, but abandoned it in the name of flexibility in the aftermath of the 2001 recession.

Flexibility is great, most of the time. But as Greece vividly demonstrates, any country that doesn't discipline itself is bound to be disciplined eventually by the bond market. And that's a whole lot more painful. | BW |

–With Maria Petrakis, Natalie Weeks, Svenja O'Donnell, and David Tweed in Athens, Stanley Reed in London, and Carol Matlack in Paris

Business Exchange

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You Can't Have It All

Turmoil in the euro zone has reawakened interest in a theory put forth in 2007 by Harvard University economist Dani Rodrik. In a post on his blog, Rodrik argued that "democracy, national sovereignty, and global economic integration are mutually incompatible." It's possible to have any two, but not all three, he wrote, calling this "the inescapable trilemma of the world economy."

To read the post, go to **http://bx.businessweek.com/global-economy/reference/**

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Google's New Billion-Dollar Baby

Display advertising, most of it on YouTube, is surging, helping to offset a slowdown in the growth of search

By Douglas MacMillan

BW 50

Google has long been criticized for relying too heavily on one source of revenue, but it may soon have its first billion-dollar business outside of search advertising. Analysts predict revenues from the company's display advertising business will rise as much as 40% this year, to slightly







more than $1 billion. Most of that business will come from selling video and banner ads on YouTube, which Google acquired in 2005.

There is some urgency behind Google's efforts to expand into display. The U.S. search advertising market is expected to grow only 5.6% this year, to $11.4 billion, according to researcher eMarketer, and Google has so much of the business it may struggle to grab more share. Display advertising, on the other hand, is projected to rise 8.2%, to $7.9 billion, and Google has only a small slice of the business. "You have to go somewhere else to get the next legs of growth," says Jim Friedland, an analyst at Cowen & Co.

While Google lags well behind leaders such as Yahoo! in display advertising, it's beginning to figure out how to use its strength in search to bolster the newer business. People conducted 2.8 billion searches on Google each day in December, according to the market research firm comScore. "Our goal is to bring the science of search to the art of display," says Neal Mohan, the executive in charge of Google's display business.

Companies often use display ads to raise awareness of a brand or product. They rely on search ads to encourage customers to take a specific action—for instance, click on a Web site or make a purchase. Because search ads are cheaper and their effectiveness easier to measure than display ads, budget-conscious advertisers flocked to them during the recession. Now display is getting a boost because big advertisers are beginning to shift money to the Web from TV and print. "There's a lot of money to be tapped that otherwise would be allocated to TV," says Greg Sterling, founder of the research firm Sterling Market Intelligence.

HAND-HOLDING

Google is developing tools to help the newcomers create more effective ads and automate their placement. It will soon roll out technology that will customize the colors, language, and other elements of a banner ad, depending on who is viewing it. Google also is helping advertisers measure the effectiveness of display ads. One Google product, Campaign Insights, correlates data from display ads and Web searches.

Hair Club, best known for its Hair Club for Men TV testimonials, was one of the first to try Campaign Insights. The tool tallied the number of people who saw Hair Club display ads on various Web sites and then went on to perform related searches. "Display [advertising] drives searches and Web site visits," says Luke Hubbard, vice-president of Integrated Media Solutions, the Beverly Hills (Calif.) ad agency that coordinated the campaign. "We knew that effect was there before, but now we are able to quantify it." Hair Club increased its spending on display ads for 2010, and Integrated Media has signed up seven other clients to use Campaign Insights. Google offers the service free to advertisers that spend above a certain amount on other products.

While Google's search ad business is largely automated, display advertising involves "a lot of hand-holding and schmoozing," says Sterling, the analyst. Amy Curtis-McIntyre, a senior vice-president at hotel chain Hyatt, says Google is getting better at the personal side of sales. The company regularly sends reps to her Chicago office. "When they develop new search tools or new advertising tools, they bring them to us and present them in a usable way," says Curtis-McIntyre.

Analysts expect Google's display ad revenues will jump as much as 40% this year

With $1 billion in sight, how big can Google's display business get? The company is "well-positioned to be a winner here," says Cowen's Friedland. The question he's now asking: "Is this a $10 billion business?" |BW|

87.8 billion

Number of Google searches in December

Data: comScore

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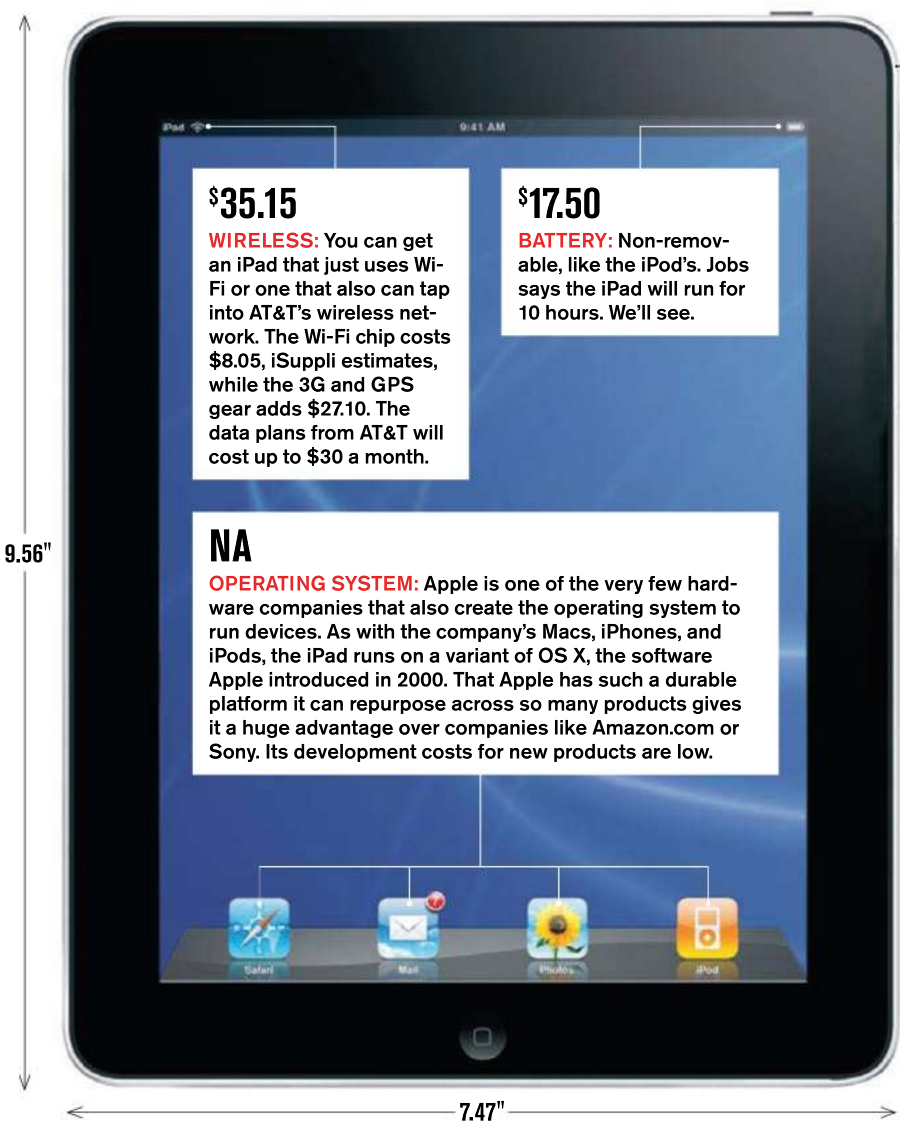
The iPad: More Than the Sum Of Its Parts. $270 More, Actually

Money is (almost) no object to early adopters, but how low can Apple go in adjusting the price of its new tablet? Here's an up-close look into the cost of making one

By Arik Hesseldahl

It'll be six weeks before anyone really knows whether the Apple iPad, unveiled last week, is "awesome" (Steve Jobs' description) or "sucks" (36,900 occurrences in a Google search). When the device goes on sale in late March, rest assured that a lot of people will buy iPads to find out for themselves. Analyst Gene Munster of Piper Jaffray estimates Apple will sell 3 million to 4 million iPads in its first year.

And Apple's price will likely be at least $269.95 higher than what it's spending on the ingredients for an iPad. That's the parts-price gap on its base $499 model, estimates the research firm iSuppli. With gross margins starting at 54%, the iPad would be the envy of the computer business and probably has room to get cheaper in the future. Apple spokesman Colin Smith declined comment. Below is iSuppli's price breakdown of some of the iPad's parts:



$35.30
ALUMINUM CASE AND BODY

$29.50 to $118
MEMORY: $29.50 for the 16 GB model to $118 for the 64 GB

$80
DISPLAY: The 9.7-inch color touchscreen will likely come from three vendors, including LG Display and Innolux, says iSuppli.

$17
PROCESSOR: Unlike most hardware companies, Apple designs its own processors so it can customize them to its particular needs. The A4 chip in the iPad was probably designed by the low-power specialist PA Semi that Apple acquired in 2008 and manufactured by Samsung, iSuppli says. The device will run iPhone applications, like Pandora Radio and Glow Hockey, and work as an electronic reader for books from publishers such as Simon & Schuster and Penguin.

Not included (because they're not elements of the iPad, to the disappointment of fanboys the world over): camera and Adobe Flash software

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No Time to Rest at UBS

The Swiss bank is profitable again—but CEO Grübel still needs to stem the exodus of wealthy clients

By Elena Logutenkova

Oswald J. Grübel gave a dazzling performance as head of Credit Suisse from 2004 to 2007, doubling the Swiss bank's profit and share price. Now, Grübel, 66, has come out of retirement for an even more challenging role. His encore performance: CEO of UBS, Switzerland's largest bank, which racked up $57.3 billion in losses during the credit crisis—more than any other European financial institution.

Since taking the job in February 2009, Grübel has garnered some good reviews. He has cut about 11,000 jobs worldwide, appointed five new managers to the executive board, started weekly calls with top risk officers, and raised $3.6 billion from investors. On Feb. 9, UBS reported its first quarterly profit in more than a year. It's expected to earn $5.14 billion in 2010, the first annual profit since 2006, according to a Bloomberg survey of 20 analysts.

The CEO has made no progress, however, on the bank's most pressing problem: withdrawals by wealthy clients, who have removed $214 billion over the past seven quarters. The outflow increased in the fourth quarter and will probably continue, analysts say, as uncertainty persists about the outcome of U.S. efforts to investigate alleged tax evasion by UBS clients. Several former UBS bankers have pleaded guilty or been indicted for helping wealthy Americans evade taxes, and the bank settled a Justice Dept. lawsuit by agreeing to cooperate and paying a $780 million fine.

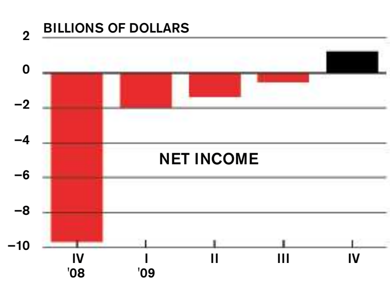
Grübel, known as "Ossie," says he is counting on the return to profitability to help make UBS "a trusted bank" again. But he hasn't announced a detailed plan to stem the bleeding or reach his goal of eventually attracting $50 billion a year in new cash to the wealth management unit. Even hitting that lofty target wouldn't bring UBS back to the glory days before the credit crisis; wealth management pulled in about $113 billion in 2007 and $87 billion in 2006.



Grübel came out of retirement to run UBS

BACK IN BLACK

UBS reported its first quarterly profit in more than a year



Data: Bloomberg

UBS's tax dispute with the U.S. will only complicate Grübel's task (page 44). In August the bank agreed to provide account data on as many as 4,450 American clients to settle an IRS summons. The Swiss administrative court muddied the picture last month by blocking the government from passing some of the data to U.S. authorities; judges ruled that the failure to file certain IRS tax forms, a key part of the UBS settlement, wasn't considered fraud in Switzerland. Both countries are working to resolve the dispute. UBS has said it is "fully supportive" of the efforts.

For now, analysts seem willing to give UBS's chief the benefit of the doubt. "Grübel has done what he said he would do," says Teresa Nielsen of asset manager Vontobel Holding. "All divisions are profitable, and now UBS needs to work on its image and reputation. It takes time."

Grübel, a war orphan who was raised by his grandparents in East Germany and never went to university, isn't afraid to shake things up. At Credit Suisse, where he spent 37 years, Grübel started cutting the bank's holdings of U.S. subprime mortgage bonds in 2006, while UBS was still buying them. Before becoming CEO of Credit Suisse, he completed a successful overhaul of private banking, adding more hedge funds and alternative investments to the group's lineup. And he showed good instincts. After meeting Bernard Madoff in 2000, he advised clients to steer clear of him.

Should Grübel work similar magic at UBS, investors could see a rich payday. The stock has fallen 9% since the end of 2008, while Credit Suisse shares climbed 60%. "UBS was a catastrophe," says Eric Bendahan, who manages $2.5 billion in the Oyster European Opportunities Fund. "But if things get back to normal, the potential is colossal." |BW|

PHOTOGRAPH BY SASKIA ROSSET/PIXSIL; CHART BY DAVID FOSTER

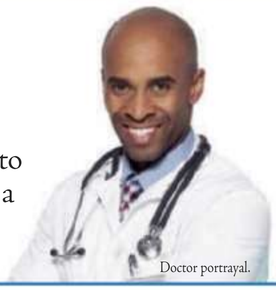
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"I was originally too embarrassed to have 'the talk' with my doctor, but now I wish I'd done it sooner."

Your Doctor Talks to Men About ED Every Day

Your doctor will tell you that erectile dysfunction (ED) isn't something to keep to yourself, or to be embarrassed about. It's a common medical condition he can treat.



Doctor portrayal.

Running the Numbers

Did you know half of all guys over 40 have some form of ED? Here are some numbers to keep in mind from a recent survey of men with ED:

71% of men were anxious about talking to their doctor about ED.

89% of men felt relieved after talking to their doctor.



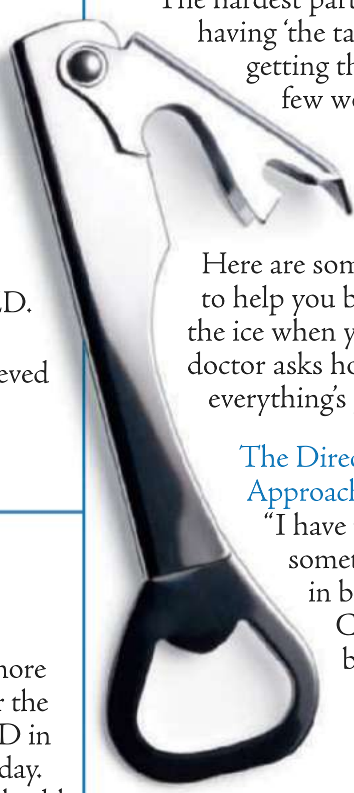
Tell Me More

To learn more about VIAGRA for the treatment of ED, and ED in general, visit **viagra.com** today. You'll find an online sexual health quiz, videos of guys with ED who've had the VIAGRA Talk and other helpful information.

Over 20 million men have already had their VIAGRA Talk. Isn't it time you had yours?

Don't Keep Your Questions Bottled Up

The hardest part about having 'the talk' is getting those first few words out.



Here are some ideas to help you break the ice when your doctor asks how everything's going:

The Direct Approach:
"I have trouble sometimes in bed. Could it be ED?"

The Indirect Approach:
"Is it true age affects sexual performance?"

The Silent Approach:
Just hand this ad to your doctor, he'll take it from there.

Important Safety Information

We know that no medicine is for everyone. Don't take VIAGRA if you take nitrates, often prescribed for chest pain, as this may cause a sudden unsafe drop in blood pressure.

Talk with your doctor first. Make sure your heart is healthy enough to have sex. If you have chest pain, nausea, or other discomforts during sex, seek medical help right away.

As with any ED tablet, in the rare event of an erection lasting more than four hours, seek immediate medical help to avoid long-term injury.

In rare instances, men who take PDE5 inhibitors (oral erectile dysfunction medicines, including VIAGRA) reported a sudden decrease or loss of vision, or sudden decrease or loss of hearing. It is not possible to determine whether these events are related directly to these medicines or to other factors. If you experience any of these symptoms, stop taking PDE5 inhibitors, including VIAGRA, and call a doctor right away.

The most common side effects of VIAGRA are headache, facial flushing, and upset stomach. Less common are bluish or blurred vision, or being sensitive to light. These may occur for a brief time.

VIAGRA does not protect against sexually transmitted diseases including HIV.

Please see Important Facts for VIAGRA on the following page or visit viagra.com for full prescribing information.

For free information, including questions to ask your doctor, call 1-888-4VIAGRA (1-888-484-2472).

VIAGRA®
(sildenafil citrate) tablets

You are encouraged to report negative side effects of prescription drugs to the FDA. Visit www.FDA.gov/medwatch or call 1-800-FDA-1088.

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IMPORTANT FACTS

VIAGRA® *(sildenafil citrate)* tablets (vi-AG-rah)

IMPORTANT SAFETY INFORMATION ABOUT VIAGRA

Never take VIAGRA if you take any medicines with nitrates. This includes nitroglycerin. Your blood pressure could drop quickly. It could fall to an unsafe or life-threatening level.

ABOUT ERECTILE DYSFUNCTION (ED)

Erectile dysfunction means a man cannot get or keep an erection. Health problems, injury, or side effects of drugs may cause ED. The cause may not be known.

ABOUT VIAGRA

VIAGRA is used to treat ED in men. When you want to have sex, VIAGRA can help you get and keep an erection when you are sexually excited. You cannot get an erection just by taking the pill. Only your doctor can prescribe VIAGRA.

VIAGRA does not cure ED.

VIAGRA does not protect you or your partner from STDs (sexually transmitted diseases) or HIV. You will need to use a condom.

VIAGRA is not a hormone or an aphrodisiac.

WHO IS VIAGRA FOR?

Who should take VIAGRA?

Men who have ED and whose heart is healthy enough for sex.

Who should NOT take VIAGRA?

- If you ever take medicines with nitrates:
  - Medicines that treat chest pain (angina), such as nitroglycerin or isosorbide mononitrate or dinitrate
- If you use some street drugs, such as "poppers" (amyl nitrate or nitrite)
- If you are allergic to anything in the VIAGRA tablet.

BEFORE YOU START VIAGRA

Tell your doctor if you have or ever had:

- Heart attack, abnormal heartbeats, or stroke
- Heart problems, such as heart failure, chest pain, or aortic valve narrowing
- Low or high blood pressure
- Severe vision loss
- An eye condition called retinitis pigmentosa
- Kidney or liver problems
- Blood problems, such as sickle cell anemia or leukemia
- A deformed penis, Peyronie's disease, or an erection that lasted more than 4 hours
- Stomach ulcers or any kind of bleeding problems

Tell your doctor about all your medicines. Include over-the-counter medicines, vitamins, and herbal products. Tell your doctor if you take or use:

- Medicines called alpha-blockers to treat high blood pressure or prostate problems. Your blood pressure could suddenly get too low. You could get dizzy or faint. Your doctor may start you on a lower dose of VIAGRA.
- Medicines called protease inhibitors for HIV. Your doctor may prescribe a 25 mg dose. Your doctor may limit VIAGRA to 25 mg in a 48-hour period.
- Other methods to cause erections. These include pills, injections, implants, or pumps.

POSSIBLE SIDE EFFECTS OF VIAGRA

Side effects are mostly mild to moderate. They usually go away after a few hours. Some of these are more likely to happen with higher doses.

The most common side effects are:

- Headache
- Feeling flushed
- Upset stomach

Less common side effects are:

- Trouble telling blue and green apart or seeing a blue tinge on things
- Eyes being more sensitive to light
- Blurred vision

Rarely, a small number of men taking VIAGRA have reported these serious events:

- Having an erection that lasts more than 4 hours. If the erection is not treated right away, long-term loss of potency could occur.
- Sudden decrease or loss of sight in one or both eyes. We do not know if these events are caused by VIAGRA and medicines like it or caused by other factors. They may be caused by conditions like high blood pressure or diabetes. If you have sudden vision changes, stop using VIAGRA and all medicines like it. Call your doctor right away.
- Sudden decrease or loss of hearing. We do not know if these events are caused by VIAGRA and medicines like it or caused by other factors. If you have sudden hearing changes, stop using VIAGRA and all medicines like it. Call your doctor right away.
- Heart attack, stroke, irregular heartbeats, and death. We do not know whether these events are caused by VIAGRA or caused by other factors. Most of these happened in men who already had heart problems.

If you have any of these problems, stop VIAGRA. Call your doctor right away.

HOW TO TAKE VIAGRA

Do:

- Take VIAGRA only the way your doctor tells you. VIAGRA comes in 25 mg, 50 mg, and 100 mg tablets. Your doctor will tell you how much to take.
- If you are over 65 or have serious liver or kidney problems, your doctor may start you at the lowest dose (25 mg).
- Take VIAGRA about 1 hour before you want to have sex. VIAGRA starts to work in about 30 minutes when you are sexually excited. VIAGRA lasts up to 4 hours.

Don't:

- Do not take VIAGRA more than once a day.
- Do not take more VIAGRA than your doctor tells you. If you think you need more VIAGRA, talk with your doctor.
- Do not start or stop any other medicines before checking with your doctor.

NEED MORE INFORMATION?

- This is only a summary of important information. Ask your doctor or pharmacist for complete product information OR
- Go to **www.viagra.com or call (888) 4-VIAGRA (484-2472).**

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Health Reform Is Dead. Let's Go Shopping

Thriving insurers and hospital chains may start to gobble up competitors weakened by the recession

By Alex Nussbaum and Meg Tirrell

As a herd of health-care proposals lumbered through Congress last year, insurers and hospital chains made like big-game hunters, shooting to kill the most sweeping provisions. With great difficulty, health-care companies and their lobbyists negotiated deals they could live with. But now that the overhaul is in deep freeze, how does the future look? Painful, for some. For others, it's a buying opportunity.

If a comprehensive health reform bill had passed, it might have pulled in more than 30 million new paying customers. Without the influx, health care companies are scrambling to cut costs—and the strongest are poised to devour the weak. Giant insurers such as WellPoint, UnitedHealth, and Aetna are on the prowl, along with hospital chains such as Community Health Systems. Consolidation is the easiest way "to spread rising costs across fewer customers," says Paul H. Keckley, executive director of the Deloitte Center for Health Solutions.

President Barack Obama's original vision called for expanding insurance coverage while toughening regulations to improve care and force down costs. The plan was upended when Republican Scott Brown won the late Edward Kennedy's Massachusetts Senate seat. Obama has since pushed to restart talks on an overhaul, but prospects appear dim.

So change must come from individual companies, and many are already signalling their intentions. WellPoint, the largest health plan by enrollment, owns 14 state Blue Cross plans. It now sees "a unique opportunity" to acquire more as small players come under pressure, CEO Angela F. Braly recently told investors. UnitedHealth, the second largest, has expanded into new businesses and purchased the Northeast unit of rival Health Net. CEO Stephen J. Hemsley told analysts in January that he has no plan to alter this strategy.

$2.5 trillion

U.S. health-care spending in 2009

Data: U.S. Centers for Medicare and Medicaid Services

Hospitals, meanwhile, continue to see their emergency rooms flooded with uninsured patients. Uncompensated for that care, many face bankruptcy. "Absent reform, fewer and fewer Americans are going to be able to afford their services," said Jacob Hacker, a Yale University political science professor, in an e-mail.

According to the American Hospital Assn., one-third of the nation's community hospitals had operating losses in 2008. In light of health reform's failure, Community Health Systems, Health Management Associates, and LifePoint Hospitals —all of them leading chains—say they are intensifying their pursuit of recession-weakened competitors. Prices for hospitals have dropped by 50% over three years, says Health Management Senior Vice-President Robert E. Farnham. LifePoint CEO William F. Carpenter III says his chain may buy three more hospitals this year.

In the months ahead, cost pressures are only going to increase. One in five working-age Americans lacked health coverage during the first half of 2009, the highest in six years, according to the U.S. Centers for Disease Control & Prevention. This has the effect of funneling patients with serious, late-stage illnesses into emergency rooms—an expensive alternative to early treatment. Last year health-care spending rose 6% over 2008, to an estimated $2.5 trillion, according to the U.S. Centers for Medicare & Medicaid Services.

If legislation can't bring costs down, consolidation might. It "allows you to operate more efficiently," notes Curtis S. Lane, senior managing director at MTS Health Partners, a New York-based equity fund. "Whether reform is imposed by the government or driven by market forces, these companies are going to have to get better at being more cost effective and providing higher quality." |BW|

ILLUSTRATION BY ROBERT NEUBECKER

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Is China Fed Up With The Colonel's Chicken?

Mainland same-store sales at KFC and Pizza Hut are down. Why that's a troubling sign for Western fast food

By Bruce Einhorn and Wing-Gar Cheng
HONG KONG

Yum! Brands has done remarkably well in the battle to win Chinese hearts and bellies, but some investors are now wondering whether the fast-food giant is faltering. Fears that Chinese tastes may be shifting away from Yum's KFC and Pizza Hut chains have hobbled the company's shares. Yum earned $216 million on global sales of $3.36 billion in the fourth quarter, with China revenue up by 8%. Sales at Chinese outlets that have been open for more than a year, though, were off for a third consecutive quarter, dropping 3%. Jitters about what Deutsche Bank describes as "stubbornly weak sales in China" helped send Yum stock down more than 6% in the two days after the company announced its results on Feb. 3.

Yum Chairman David C. Novak says he's not worried: "If this is a problem, it's a Class A problem." Novak points to the company's many successes in China and blames the same-store sales decline on the lousy global economy.

KFC hit the mainland in 1987, three years ahead of the first Golden Arches. While McDonald's tried to convince skeptical Chinese to buy hamburgers, KFC and Pizza Hut spiced up their menus with barbeque squid, egg tarts, and other goodies tailored to local tastes. Today, Yum is China's top restaurant operator, with more than 3,400 outlets, and the country accounts for 36% of total sales, just behind the U.S. "When the consumer rebounds [in China]," Novak says, "we're well placed."

"WE'LL HAVE THREE RESTAURANTS IN A CITY BEFORE McDONALD'S EVEN GETS THERE," SAYS YUM'S CHAIRMAN



KFC in Qingdao: Menus tailored to local tastes have been key to Yum's success

But some analysts think China may be saturated with Western brands, especially in big cities. "There's nothing particularly novel about [foreign products] anymore," says Jason Li, CEO of Yatsen Associates, a Beijing consulting firm. Selina Sia, a researcher at Mirae Asset Securities in Hong Kong, says that while Chinese embraced American fast food a decade ago, that's changing. "It's good for a while," she says, "but then they go back to their own diet."

Yum faces stronger competition from local rivals, too. "Ten, fifteen years ago, if you had air-conditioning with a clean bathroom, you were unique," says Joel Silverstein, president of East West Hospitality, a Hong Kong consulting firm. Now, Chinese chains are cleaning up and expanding, often with help from global investors. U.S. private equity giant Carlyle Group bought into Babela's Kitchen, a Shanghai-based Italian chain. London-based Actis Capital controls Xiabu Xiabu, a hot pot (or Chinese fondue) chain headquartered in Beijing. And Jollibee, the top fast-food player in the Philippines, owns two Chinese chains.

McDonald's, meanwhile, is refocusing in China. It plans to open as many as 175 new mainland restaurants this year, vs. about 140 in 2009. The chain will spruce up some of its dowdier restaurants and offer free Wi-Fi. One thing it won't do is follow Yum's lead and make big changes to the menu to suit local tastes, says McDonald's China boss, Kenneth Chan. While a few additions are possible, he says the Chinese enjoy "Big Macs, our chicken sandwiches, and our French fries."

Yum knows it needs to keep moving. The company is adding more breakfast items at KFC; it's expanding the menu and introducing afternoon tea and coffee at Pizza Hut; it has opened 19 Chinese restaurants called East Dawning; and in October, Yum agreed to pay $40 million for a 7.3% stake in Little Sheep, a chain of hot pot restaurants. This year, Yum expects to open more than 500 outlets in China, says Novak, and it is expanding into smaller cities in the interior. "We'll have three restaurants in a city," he promises, "before McDonald's even gets there." | BW |

–With Wendy Leung in Shenzhen

WU HONG/EPA/CORBIS

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Obama: "We want and need more input from the corporate community"

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OBAMA'S CORPORATE MESSAGING

Two things troubled President Barack Obama as he greeted *Bloomberg BusinessWeek* on Feb. 9 for a wide-ranging interview in the Oval Office. First was the snowstorm that had crippled Washington. "I can't believe I have to shut down the federal government for a week for this," said the President, gazing outside in mock condescension before reminiscing about his years in Chicago, a city that takes heavy weather in stride. Obama's second concern is more frustrating and far less likely to melt away: the impression that his Administration—and he personally—is anti-business.

At least on this day, business and the economy topped Obama's agenda. Twenty steps from the Oval Office, GE's Jeff Immelt, Honeywell's David Cote, and several other CEOs huddled with White House officials to provide industry input on climate change. With his economic council waiting outside, Obama repeatedly expressed his disappointment that policies he believes are overwhelmingly pro-business have been misunderstood. Obama even had a staffer send a follow-up e-mail to a question about CEOs he admires with additional names, including Cote, Verizon's Ivan Seidenberg, and John Doerr of Kleiner Perkins Caufield & Byers.

What follows are excerpts of Obama's conversation with Bloomberg News White House Correspondent Julianna Goldman, Washington Bureau Chief Michael Tackett, Executive Editor Albert Hunt, and *Bloomberg BusinessWeek* Editor Josh Tyrangiel.

BLOOMBERG BUSINESSWEEK
There is a sense that the Administration is perceived as anti-business. Why?

PRESIDENT OBAMA
I think that is a good question, because if you actually look at our policies, everything that we have done over the last year, and everything we intend to do over the next several years, I think is going to put American business on a stronger footing.

Look, I came in with the worst economic crisis and financial crisis we have had since the 1930s, significantly worse than what we saw in the 1980s. And the steps that we took were designed to break the back of the recession, put a floor under the economy, and reduce a sense of panic that had grown. And I think we have done that very successfully. We had an economy that was contracting by 6%. It is now growing by 6%. We had a market that people had no idea where it would bottom out, and that market has now stabilized. We had a banking system that was on the verge of meltdown that now is showing significant health, at least in terms of their bottom lines. And so the steps we have taken, I think, has created an environment in which businesses can be profitable.

Photograph by Marco Grob

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And yet, that perception seems to still be out there.
Yes. I think that part of what has happened is that during the course of the year, the frustrations expressed toward the behavior of some of the biggest banks on Wall Street—a frustration that was not unique to my Administration but is widely shared across the country—in the minds of a lot of business leaders was viewed as anti-business rhetoric. And I think that part of what also happened was that there were some big issues like health reform, like energy, like financial regulatory reform, in which you have got some pretty significant, well-funded industry interest groups who are adamantly opposed. And they have got a lot of sway within the business community.

Some of that anti-Wall Street rhetoric is heard by businesspeople outside of Wall Street. Do you think that they take that as a lack of confidence and, therefore, they are hesitant to invest?
I do think that the anger directed toward the big banks had a spillover effect. As much as we have actually been restrained this year, if you look at the statements coming out of this White House, the irony is, is that on the left we are perceived as being in the pockets of Big Business. And then on the business side, we are perceived as being anti-business.

We are pro-growth. We are fierce advocates for a thriving, dynamic free market. But we do think that there have to be some rules of the road in place in the financial sector that will create an even playing field and allow businesses to raise capital and consumers to buy products with confidence.

Coming out of this past decade, there has been a sense on the part of a lot of middle-class families that they have been left behind, even when we were expanding. And I talked during the campaign about the need for us to restore a sense of balance to the compact between business, government, and employees all across the country.

If businesses are making record profits but employees are seeing their wages flatline—and in fact, incomes decline over the course of the decade—that puts enormous strains on families. It puts, I think, a dampening effect on consumers who help drive this economy. We are going to be better off if everybody feels like they have got a stake in growth and innovation moving forward. And I think that balance got lost.

Now, making sure that we restore that balance without tipping too far in the other direction in ways that squelch innovation and investment is going to be an important challenge, and one that we take very seriously. But the important message I would have for the business community—and this is something that I emphasize every time I have lunch with CEOs, and we have had a lot of them in here—is we have every interest in you succeeding.

In the international marketplace, the more the American brand and American products and American services are thriving, the better off we are going to be and, by the way, the better off I will look as President of the United States.



> On Dimon's and Blankfein's bonuses :

"I KNOW BOTH THOSE GUYS. THEY ARE VERY SAVVY BUSINESSMEN. AND I, LIKE MOST OF THE AMERICAN PEOPLE, DON'T BEGRUDGE PEOPLE SUCCESS OR WEALTH"

CHIP SOMODEVILLA/GETTY IMAGES

Every American President in the last 30 years has had a major CEO as a member of the Cabinet in the inner circle. You don't so far. Why is that?
It just has to do with who the particular individuals who were needed at a time of crisis. I thought it was very important to have Larry Summers and Tim Geithner as two of my key economic advisers early on because they had gone through significant global economic crises before.

But I think it is a legitimate point to say that we want and need more input from the corporate community, if nothing else, just so that we can communicate to the corporate community and to the business community the fact that, if you look at our actual policies, as opposed to the speculation around our policies, they have been fundamentally business-friendly.

Do you want to weigh in on a specific CEO you admire?
There are a bunch of them. You know who I really enjoyed talking to at our last lunch was Fred Smith of FedEx. Very thoughtful. He's an example of somebody who is thinking long-term. His industry is deeply sensitive to energy prices, and he's the first one to say that if we don't start getting an energy policy that's smart, we're going to lose. He's also very thoughtful about trade and talks about the difficulties they've had in some cases with partners around the world. Obviously, along with UPS and some other U.S.-based companies, they're the best in the world at logistics and moving product. That's something that we should be able to export to other countries, and we're having a lot of problems with it. But that's just one example of somebody where sitting down and talking to him was incredibly productive and helps inform how we shape policy.

If you had to distill your economic message into a single declarative sentence, what would it be?
That having broken the back of this recession, our goal now is to build a new foundation for long-term, sustainable economic growth, and that that requires innovation. It requires a smart energy policy. It requires a health-care system that is not a drag on business. And it requires an education system that is producing the most productive workers in the world.

You proposed a payroll tax [credit] for small businesses that boost hiring. Would you consider expanding that to all hiring?

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We think that small businesses are the area where a targeted jobs credit would make the most difference right now. We think bigger businesses that have healthier balance sheets, more money, are in a position right now to hire, and that their decisions are going to have more to do with, are they seeing enough customers out there to justify expanding payroll.

I am optimistic that in the months to come you are going to see more and more investment like that, people being willing to take additional workers on. But small businesses are still having problems, even where they are seeing more orders, they are still having problems just generating enough capital to be able to take on more workers.

And we think that a jobs credit might not have been appropriate in the depths of the recession, where just because of the lack of demand, people were not going to hire no matter what. They were just trying to hang on. Now, as the economy is recovering, a job credit can potentially accelerate people who may be planning to hire at some point, anyway, but right now are just dipping their toe in the water.

If your deficit commission comes back and says we would recommend raising taxes on households earning less than $250,000 a year, would you accept that as part of a larger deal?
I don't want to prejudge the commission because the whole point of it is to make sure that all ideas are on the table, and let's see what folks can come up with.

What I want to do is to be completely agnostic in terms of solutions. I want everybody to sit down and work off of a common base of facts. And the fact of the matter is that we have a structural deficit that is in place that was there before the recession. The recession has compounded it.

But our real problem is not the spike in spending last year or even the lost revenues last year, as significant as those are. The real problem has to do with the fact that there is just a mismatch between the amount of money coming in and the amount of money going out. And that is going to require some big, tough choices that, so far, the political system has been unable to deal with.

Let's talk bonuses for a minute. Lloyd Blankfein: $9 million. Jamie Dimon: $17 million. Now, those were in stock and less than what some had expected. But are those numbers O.K.?
First of all, I know both those guys. They are very savvy businessmen. And I, like most of the American people, don't begrudge people success or wealth. That is part of the free-market system.

I do think that the compensation packages that we have seen over the last decade, at least, have not matched up always to performance. I think that shareholders oftentimes have not had any significant say in the pay structures for CEOs.

Seventeen million is a lot for Main Street to stomach.
Listen. $17 million is an extraordinary amount of money. Of course, there are some baseball players who are making more than that and don't get to the World Series either, so I am shocked by that as well.

I guess the main principle we want to promote is safe say on pay, that shareholders have a chance to actually scrutinize what CEOs are getting paid, and I think that serves as a restraint and helps align performance with pay. The other thing we do think is the more that pay comes in the form of stock that requires proven performance over a certain period of time, as opposed to quarterly earnings, is a fairer way of measuring CEO success and, ultimately, will make the performance of American businesses better.

The Volcker Rule got a bit of a frosty reception from the Senate Banking Committee. Has the bank lobby rolled you on this one already?
(Laughs) Let me broaden the question, and then I will get specifically to the Volcker Rule.

After what we have gone through, surely nobody in the business community thinks that the status quo, in terms of how we regulate the financial system, is adequate. I can't believe that there is anybody who is running a business out there who thinks that 60-to-1 leverage and folks making $100 million bonuses based on gambles on derivatives, takes comfort in that kind of system.

What we have said is that if you look at the holes in the system right now, we have got to have a way of monitoring the systemic risks. We have got to make sure that there is a way to wind down a firm that's in trouble that is quarantined from the rest of the system so that we don't have institutions that are too big to fail.

We think it is very important to have a consolidated and streamlined regulatory approach to things like derivatives and hedge funds, not just banks. We think it is important to have a consolidated and streamlined approach to consumer financial protection, because although it is true that the immediate cause of Lehman's [bankruptcy] may not have had to do with what was going on with credit cards, what is also true is that if you have consumers who are getting predatory loans that they don't



KEVIN LAMARQUE/REUTERS

> On the Volcker Rule and financial reform:

"I CAN'T BELIEVE THAT THERE IS ANYBODY WHO IS RUNNING A BUSINESS OUT THERE WHO THINKS THAT 60-TO-1 LEVERAGE AND FOLKS MAKING $100 MILLION BONUSES BASED ON GAMBLES ON DERIVATIVES, TAKES COMFORT IN THAT KIND OF SYSTEM"

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understand, credit cards or debit-card rates that they don't understand, a lot of these financial instruments that drive huge profits, but leave consumers unprotected. That is not good for the system overall.

We think that increasing capital requirements for systemically significant firms is important. So all these things are of a piece—not designed to squelch innovation in the financial market, but



› *On the importance of new trade pacts:*

"FRANKLY, WE HAVE GOTTEN OUR CLOCK CLEANED OVER THE LAST SEVERAL DECADES WHEN IT COMES TO WORLD TRADE"

designed to make sure that there is a level playing field, transparency, clarity in how this system operates.

Now, the Volcker Rule is part of this overall framework. And I think there has been some misunderstanding, at least in the popular press, about what we are proposing. What we are simply saying is that it makes sense if banks are getting cheap money through the discount window, if they've got assurances and guarantees from the government, that they don't simply take that cheap money, fully backed by the U.S. Treasury, and go out and just start rolling the dice in proprietary trading or other transactions that aren't designed to help raise money for their customers or designed to ensure investment and job growth, but basically, are just designed to boost their profits and their bonuses.

That is not something the government probably should be in the business of subsidizing. And that is the essence of the rule.

Whether we can get it through Congress is always a question because, as we have seen throughout this year, we have a political process in Washington right now that is a little dysfunctional.

You want to double exports over the next five years. What about trade agreements with South Korea, Colombia, and Panama? Will you press Congress this year to sign any or all of those agreements?
I would like to get them done. And, now, whether I can get all three done or any one of them done this year, in part, is going to depend on the conversations between our U.S. Trade Representative and his counterpart in those three other countries.

In each of those countries there are different glitches in getting a deal completed. With respect to South Korea, there is some concern that, although the deal was good for our telecommunications and our finance system, that our auto exports to South Korea are still subjected to a lot of nontariff barriers.

But this year, if you could, you would like to do that?
If we can work out those kinks in a way that is fair and reciprocal, then I would like to get them done because the vision I have for our economy in this century is that, after going through a binge where we are a consumer economy driven by home equity loans and debt, that we are making stuff and we are selling it to other countries. And we have the potential to do that, because we have still got the most innovative economy. We have still got the best universities in the world. We have still got, I think, a structure that is friendliest to entrepreneurs. But frankly, we have gotten our clock cleaned over the last several decades when it comes to world trade.

The interesting thing in conversations I'm having with CEOs now is that it is not just labor that has concerns with trade now. What you are seeing are a lot of corporate CEOs who are concerned about mercantilist practices by other countries and feel as if the U.S. is not being aggressive enough in terms of our export promotion and getting the best deal possible.

Part of what I think we need to do is to align the interests of business, and workers, and the U.S. government, recognizing that we have got to compete with these other countries. And so the old rhetoric of business is free trade no matter what—whatever the deal is—and labor is opposed no matter what the deal is, that is what I want to break.

You said you would get much tougher with China on trade. Yet so far the Administration has shied away from citing China for currency manipulation. Are you ready to do that now?
During the course of this crisis, we got the G20 to adopt language that explicitly says for the global economy to continue to grow, there has to be a rebalancing. The U.S. can't be the consumer engine for the entire world while we are racking up more and more debt.

The relationship between China and the United States is obviously key to that. And I have said publicly, and I will repeat, that China and its currency policies are impeding the rebalancing that's necessary. My goal over the course of the next year is for China to recognize that it is also in their interest to allow their currency to appreciate because, frankly, they have got a potentially overheating economy.

There are a bunch of bubbles that are being created inside of China. What you are also seeing is when China maintains a currency peg to the dollar, it is forcing other countries, particularly in Asia, competitors, to do the same and artificially devaluating its currency.

So this is something that goes beyond China, but China is the biggest player in this. And we are going to have some very serious negotiations. And it's going to be bumpy, because China's entire growth model has been based on exports rather than internal consumer demand for a very long time.

But we think that if China adjusted that policy, what you would actually see is more consumer purchasing power inside of China, a growing domestic market. They would be less vulnerable

DOMINIC NAHR/POLARIS

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to the vicissitudes of trade. And so, it is a potential win-win situation. But, look, negotiations with China, or any country, when it comes to trade and currency, is never easy.

On jobs, obviously, the American automobile industry is so important to this economy. Now we have got a situation with Toyota. Do you think that the response to the safety concerns with those cars was delayed? And if so, do you think that responsibility lay with either the regulators, the company, or both?
We don't yet know all the facts. So I don't want to offer an opinion just off the top of my head. Obviously, Toyota has been an extraordinary automaker for a very long time, and I suspect that they will continue to be, despite this recent glitch.

I do think that every automaker has an obligation when public safety is a concern, to come forward quickly and decisively when problems are identified. We don't yet know whether that happened with Toyota. That's going to be investigated. And my hope is that, moving forward, all automakers recognize that their brands are at stake when it comes to safety issues.

I will point out, while we're on the topic of autos, that Ford is doing very well and GM posted a profit. And although there was a lot of second-guessing about our interventions in these auto companies, we feel that we made the right decision. GM and Chrysler aren't out of the woods yet, but there is an enormous opportunity for us to rebuild a U.S. auto industry that, absent our intervention, might not have been there, at least with those two companies.

So that is an example of a very hard decision and a very politically unpopular decision that from my vantage point is pro-business. And my expectation is that as the economy continues to grow, more and more businesses will recognize that.

The last point I want to make with respect to just our policies on business, generally, and this goes to your first question about the perception of us being anti-business: This year I will sign legislation that will cut corporate

MARCO GROB



› *On being anti-business:*

"YOU WOULD BE HARD-PRESSED TO IDENTIFY A PIECE OF LEGISLATION THAT WE HAVE PROPOSED OUT THERE THAT, NET, IS NOT GOOD FOR BUSINESSES"

taxes by about $70 billion— their tax obligations will be reduced by about 10% because of bonus depreciation and some other steps that we intend to take. This notion, somehow, that we have been putting this enormous tax burden on business is just not true. It is not supported by the facts.

And even some of the more controversial proposals that we have put forward, like health care, if you actually analyzed what's on the table there, certainly small businesses are a net winner, one of the biggest winners. Because it would provide significant subsidies to them to provide insurance for their workers and allow them to pool with other small businesses and individuals to get a better rate. Large businesses who are already providing health insurance to their employees would end up benefiting from significant changes in delivery systems that would promise to lower costs over the long term.

You would be hard-pressed to identify a piece of legislation that we have proposed out there that, net, is not good for businesses. That doesn't mean that some people might not be happy with it, and this goes to the broader point that I was raising earlier.

I think that the two areas where we probably got the most [criticism] from the business community that are specific, as opposed to general and "we're worried about your rhetoric," one has to do with marginal rates. Now I was very clear during the campaign that for people making more than $250,000 a year, we were going to go back to the kind of rates structure that we had during Bill Clinton in the 1990s, when businesses were doing perfectly well.

I do that not for any punitive sense, but simply that I can't deal with debt and deficits in a realistic way and continue to sustain those particular tax cuts.

The second area had to do with issues of deferral and multinational practices in terms of how they deal with the tax code. We listened to some of those concerns, but the proposal that we put forward, I think, is one that the average business would say is eminently fair. If you are a business here, entirely located in the United States, and investing in the United States, and hiring workers in the United States, you are paying a 35% rate.

If you are a multinational and you are investing in India, and your workforce is in India, and your plants and equipment are in India, but your headquarters are here, you are taking deductions on all the expenses in India, but you are keeping your profits outside the United States, that just doesn't seem entirely fair. The same is true where you have companies that have 90% of their sales in the United States, but are posting 90% of their profits overseas. You get a sense there that the accountants have been busy.

Now, there are some legitimate concerns that were voiced from last year's proposal where people pointed out, well, we may be investing a lot in R&D here in the United States, but we have got to have factories or sales forces outside the United States, and you don't want to discourage [companies] from doing that. So we made modifications around some of these proposals.

But our goal here is simply to make sure that there is an even playing field between businesses who are investing in the United States, hiring U.S. workers, selling to a lot of customers here as well as overseas, and those who are operating across borders. And that is an area where there can be some legitimate debate, but certainly shouldn't be portrayed, somehow, as being anti-business. | BW |

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DETROIT'S BIG CHANCE

GM and Ford have an opportunity to steal buyers from a bloodied Toyota. The trick is not to seem predatory

By David Welch, Keith Naughton, and Burt Helm



PHOTO ILLUSTRATION BY DAVID RUDES/BW; PHOTOGRAPH BY KIMBALL STOCK COLLECTION

The pitch was so ballsy, it bordered on the laughable. An American automaker that had just emerged from bankruptcy—an endlessly beleaguered outfit that for years had been unable to build cars people wanted to buy—was launching an ad campaign that boasted, "May the Best Car Win." It was September 2009, and General Motors was in danger of leading with its chin. Robert Lutz, then the company's marketing chief, decided it was time to shock consumers. Lutz felt Americans weren't giving GM enough credit for making cars that were as good as the Japanese competition. He was proud of his new Chevrolet Malibu, his Buick LaCrosse, and his Cadillac CTS. What could be gutsier than comparing Chevys to Toyotas and Buicks to Lexuses?

Car companies have been bragging about themselves and running down their rivals forever. But it's harder to do when 61% of your company has been pawned to the federal government. GM Chairman Edward Whitacre Jr. agreed with Lutz anyway, and greenlighted the campaign created by

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Benavides tries out a Chevy Tahoe after planning to buy a Toyota Sequoia

McCann Erickson. And the GM ads that seemed so risky last summer came to seem prescient last month when Toyota Motor stumbled into the worst crisis in its history: more than 8 million cars recalled worldwide, plummeting sales, and a U.S. government investigation into whether the company should have moved faster to correct the mechanical problems of its automobiles.

UNPRECEDENTED OPPORTUNITY

When was the last time an American carmaker caught a break? More to the point, how often does one of them create its own good fortune? Both have been rare. No one could have predicted that Toyota, the company that invented *kaizen*, or continuous improvement, would flame out over quality. But now that it has, GM, Ford, and even Chrysler have an unprecedented opportunity to grab Toyota's customers. It won't be clear for some time how badly the recalls have hurt the Toyota, Scion, and Lexus brands. And Toyota, still a great company at its core, will doubtless recover some of its sheen. But it's probably fair to say that consumers will never again look at the world's largest automaker the same way.

So what's it going to be, Detroit? How far are you willing to push this? Many consumers may find it unseemly for Ford or GM to trash a bloodied competitor, even one suffering from self-inflicted wounds. That's why it's so significant that GM cooked up this approach six months ago; a company executive acknowledges that they wouldn't have dared launch the campaign after Toyota started the recall. At a moment when the industry is packing vehicles with more and more glitch-prone computers (page 42), Ford or GM could easily find themselves trapped in recall hell tomorrow. And although history may be filled with instances of companies grabbing share when their rivals are stumbling and distracted, the tricky part is doing so without appearing predatory. "Disparagement or gloating," Lutz wrote in an e-mail, "will only trigger a sympathy backlash in favor of Toyota."

For Detroit, the good news started sneaking into town in the late aughts. It showed up first at the Dearborn (Mich.) headquarters of Ford, when Alan Mulally, high-flying Boeing executive and Lexus driver, became Ford's CEO in September 2006. Mulally had studied Toyota for years and instilled its manufacturing and product development principles into Boeing's aircraft assembly. Now it was Ford's turn. Three months into the job, he made the industry equivalent of a state visit to Toyota City to see how Ford might emulate the automaker he called "the master." Upon his return, he called Toyota "the finest machine in the world, the finest production system in the world."

Mulally pushed Ford to create hotter, more sophisticated cars that would surpass Toyota's staid sedans. Ford invested billions to turn its Focus compact and Fiesta subcompact into aggressively styled small cars packed with creature comforts and powered by high-tech engines that are stingy on gas. Ford will begin selling the Fiesta in the U.S. this summer, the first subcompact in its American showrooms in years. The Focus arrives early next year. Sales of Ford's Fusion family sedan, restyled last year with a scowling face and 41-mpg hybrid system, rose 22.4% in 2009, while Toyota Camry sales fell 18.3%, according to researcher Autodata.

Mulally has been zealous about Ford's quality, too. In 2006, he delayed the launch of the Ford Edge sport wagon by a couple of months, forfeiting precious sales because he wasn't satisfied with the fit or finish. The hard work paid off. Ford now ranks in the top 10 in J.D. Power's initial quality survey—right behind Toyota. Just five years ago, Ford ranked 22nd among 41 brands and was below the industry average for problems per 100 cars. *Consumer Reports*, the buying bible for millions of tire kickers, recently praised Ford for having "world-class reliability" and now recommends 13 of its models, vs. 14 for Toyota. "Ford is ideally placed to steal away some business with all the work they've done on recent models in reliability," says David Champion, the magazine's auto editor.

Ford has even begun staking out a reputation as a technology innovator. The company that in 2004 had to license hybrid technology from Toyota (for its Escape hybrid SUV) now offers four hybrid models and an advanced voice-activated phone and entertainment system known as Sync that it developed with Microsoft. Its latest twists on technology are touchscreens that replace dashboard buttons and iPod-inspired thumbwheel controls on the steering wheel. On the airwaves, Ford has begun touting that the Fusion hybrid gets 8 miles to the gallon more than the Camry hybrid in city driving. Another spot brags, "Ford quality is equal to Honda and Toyota. If they can't beat Ford, Ford must be hard to beat."

Chevy compares the Malibu with Toyota's Camry in an ad push begun last fall



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MATTHEW GILSON

cars until the Malibu came out in 2008. Now that's changing. The new Chevy Cruze compact comes out this fall offering close to 40 miles per gallon on the highway. That beats the fuel economy of any small car Toyota sells except the Prius.

Chevy is finally getting serious about subcompacts, too. To counter Ford's Fiesta and the Toyota Yaris subcompact, GM will launch an all-new Aveo next year. It will be a more substantial car than the current version.

BRAGGING RIGHTS

Right now the General can't afford to get too cocky about the quality of its cars and trucks, though quality has improved significantly in recent years. But the electric Chevy Volt, which will start hitting the showroom this fall, could give GM something to talk about. The company says the Volt will get a 230-mpg fuel economy rating. That means the Volt will be four times as fuel-efficient as Toyota's 2010 Prius, which now has software problems with its brakes. GM says the Volt will go 40 miles on a charge before the gasoline engine kicks in. The automaker plans to sell only 10,000 of the cars next year—the Volt is more about establishing technological cred than making money. But it could take a bigger bite out of Prius sales as GM ramps up production to 60,000 a year worldwide beginning in 2012.

The good news came more slowly to GM, and it was easily overlooked amid all the dire headlines about bankruptcy and bailouts. But even industry skeptics acknowledge that over the past few years the company has put together one of the smartest design operations around. That is partly thanks to Lutz, who despite his 77 years remains indefatigable. The controversial Lutz, the "car guy" who said in 2001 that the newest concept cars looked like "angry kitchen appliances," has taken a blowtorch to GM's design-by-committee bureaucracy, sidestepped the bean counters, and begun putting a few sweet machines in the Chevy, Buick, and Cadillac lineups. The much-praised Malibu makes even the redesigned Camry look staid by comparison, and GM has been making a Very Big Deal in its TV commercials about the Buick LaCrosse's tony cockpit. "GM has had a design renaissance," says IHS Global Insight analyst John Wolkonowicz.

GM still has gaping holes in its model lineup, namely the sort of small cars Toyota has long made so well. The Detroit company was so distracted by its financial problems in recent years that it didn't invest real money into its passenger

Given Chrysler's plunging market share, it seems almost pointless to mention Detroit's No. 3 automaker, though the company, now controlled by Italy's Fiat, does have one brand that attracts some Toyota buyers. It's called Jeep. All the same, with Chrysler's quality scores near the bottom of the pile, the company will struggle to sell vehicles to Toyota owners who prize reliability.

With Ford picking up speed and GM pulling out of the pit stop, you might expect some chest-beating in Detroit. In fact, the atmosphere is one of trepidation. These folks have been down so long that they don't want to tempt fate. A GM marketing executive says he and his colleagues first discussed ways to capitalize on Toyota's woes without seeming ghoulish. After all, this person says, Toyota's problems are serious; several people have died driving models that the company subsequently recalled. As executives met to discuss the way forward,

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dealers were calling to say that Toyota customers were showing up in their showrooms and looking at GM cars. The dealers fretted that with Toyota's resale values falling, they could get burned taking a trade-in that might sell at a loss later, says one executive who asked not to be named because GM wants to keep a low profile when it comes to Toyota's problems. In late January, GM marketing executives decided to offer $1,000 to anyone wanting to trade in a Toyota for one of their cars.

Eric Hirshberg, CEO and chief creative officer of Deutsch LA, which until recently did work for GM, says the rebates "are real close to the line" in terms of taste. The better strategy for GM, he says, is to stick with its "May the Best Car Win" campaign. "The most you would do is focus on your own analogous safety strengths," he says. "People are very focused on safety. Timing is everything." Hirshberg says the American carmakers could highlight crash-test ratings or quality scores, but tactfully. "You're handling a live grenade," he says. "A whiff of opportunism or schadenfreude would be as damaging to the advertiser as this is for Toyota."

Ford has been offering $1,000 rebates, too. Few at Ford feel Toyota's pain more acutely than marketing chief James Farley, who ran the Lexus division and was a Toyota marketing executive for 17 years. "Our actions were very sympathetic to what Toyota is going through," he insists. "Our intentions weren't to be opportunistic." Still, Farley acknowledges that in the first days of the rebates Ford dealers had their best weekend in January. "The uncertainty with one of our competitors may have helped bring out some customers who felt like it was a good time to buy," he says. "People are feeling, 'Hey, it seems there's some deals out there.' " In the coming weeks and months, Ford is considering spending more on advertising in the U.S., particularly on ads that compare its cars and trucks with those offered by Toyota, says a person familiar with the plans who asked not to be identified revealing internal deliberations.

"I DON'T WANT TO BE THAT STATISTIC"

In January, Toyota's U.S. market share fell from 17.9% to 14.1% (though that was partly because it stopped selling several models). That month, Ford grabbed 16.7% of the market, up from 14.2% the previous year. Farley says Ford has been doing better lately in some regions where Toyota has long ruled the road. Although GM is in the midst of cutting its brands from eight to four, its market share jumped from 19.5% to 21% in January. If it expects to extend those gains, it will have to win over more people like Homer Benavides. The 37-year-old engineer was negotiating to buy a Toyota Sequoia in suburban Chicago when he heard the SUV was being recalled for a sticky accelerator. "Toyota produces millions of vehicles and only a fraction have the problem," says Benavides, whose wife is expecting twins. "But I don't want to be that statistic." Benavides plans to buy a Chevy Tahoe instead. Stealing back some Toyota owners who drive trucks and SUVs may be GM's best play at first, since Chevy and GMC won over those buyers long ago.

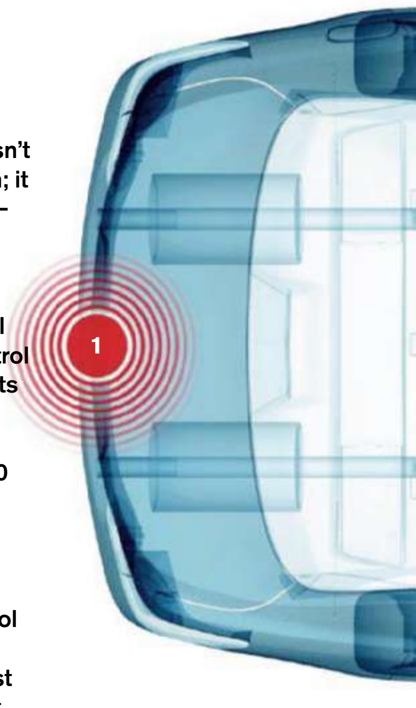
Toyota has long dominated the boomer market, and it won't be easy for Ford and GM to woo graying consumers. "There's a large group of boomers whose opinion of Toyota is very high," says Dan Gorrell, president of AutoStratagem, a California consulting firm. "They'll be unaffected by this."

However, Detroit could reel in Generation Y, which likes Toyota but is less loyal than older buyers. Ford, in particular, has an opportunity thanks to Mulally's focus on small, zippy cars such as the Fiesta and Focus, which compare favorably with such Gen Y faves as the Honda Civic and Mazda3. GM, for its part, may have more luck with the next generation. According to a survey by Strategic Visions, a market research firm in San Diego, American kids aged 12 to 16 aspire to own muscle cars such as the Ford Mustang and Chevy Corvette.

There is a lot of pent-up demand out there, and as the economy improves there will be more opportunities for Detroit to make its case to Americans. But consumer psy-

RECIPE FOR RECALLS?

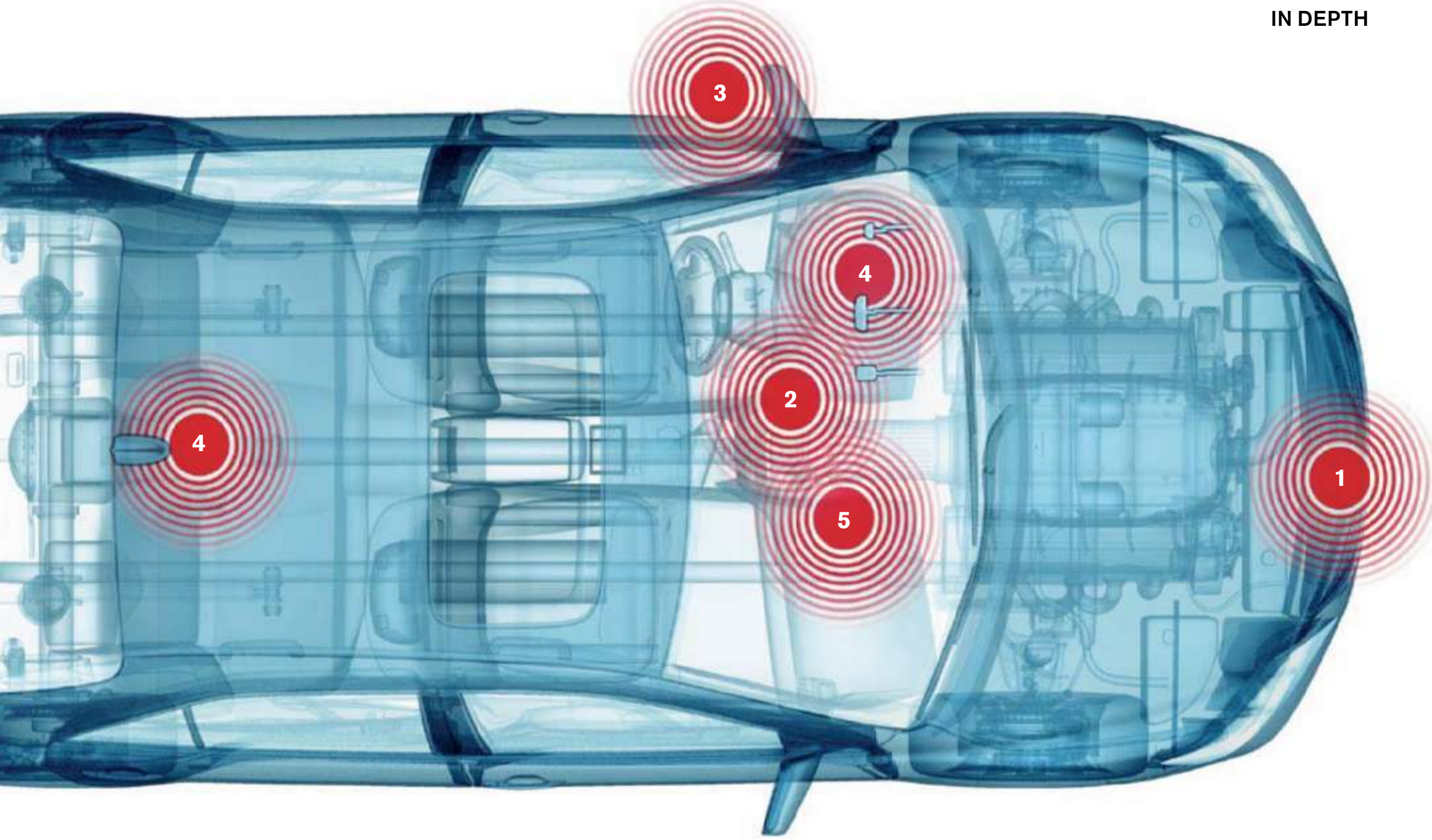
The 2010 Prius recall wasn't simply a braking problem; it was a software problem—and perhaps a harbinger of things to come. A decade ago, the average vehicle relied on a central internal computer to control everything from headlights to wipers to automatic rear lift gates. But cars today have as many as 80 microprocessors; luxury models may have 100. Some of this technology is merely convenient, giving drivers more control over entertainment and climate systems, but most of it is crucially important because these chips and software improve safety, performance, and fuel efficiency. But there's a downside: In 2007 carmakers recalled 1.2 million vehicles for software glitches, compared with 420,000 in 2003, according to research by Hughes Telematics, which makes electronics for cars. Here are five sophisticated technologies, each with the potential for recall-worthy problems.



1 ADAPTIVE CRUISE CONTROL

A refined version of the cruise control that has allowed drivers to set a desired speed since the 1950s, adaptive cruise control continuously monitors traffic and adjusts the throttle and brakes to match other cars' speed and maintain a safe distance from the car ahead. A microwave unit or laser often mounted behind the grille scans traffic and feeds the information to an onboard computer to warn the driver or even slow the car down.

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2 DRIVE BY WIRE

Most new cars employ this technology, which measures how much oomph the driver wants by reading the position of the pedal and then tells the engine how much to power up. The software boosts mpg by controlling fuel use, but has recently been implicated in lawsuits against Toyota. The plaintiffs allege that an electronic malfunction caused cars to surge forward regardless of what the driver did. Toyota denies that electronics are the problem.

3 BLIND SPOT ALERT

When sensors embedded in the side of the rear bumpers detect vehicles in a driver's blind spot, a light flashes in the mirror or an alarm beeps inside the car. The technology is generally offered as an option on luxury vehicles such as the Volvo XC90 and is making its way into mainstream models like the Ford Taurus. It's one of those technologies that can make for lazy drivers. Is looking over your shoulder really such a pain in the neck?

4 TIME FOR AN UPGRADE

After drivers take their cars in for tune-ups or repairs, the technician connects a diagnostic device to a port under the dashboard. Besides calculating what's wrong with the car, the computer uploads the latest software, just like your home PC does. The software makers want to send upgrades automatically to the car via satellite, but car companies want to maintain control, arguing that only their trained technicians can ensure that the software has been installed correctly.

5 THAT'S ENTERTAINMENT

Advances like Ford's Sync infotainment system, which can download music or access tunes in the driver's onboard library by voice command, and add-ons such as Chrysler's satellite TV for rear passengers, bring even more computing power to cars. As the industry catches up with demand and links music downloads to the dashboard, the chips and software will keep piling up. And the more cool gizmos your car has, the more chances you have for something to go haywire.

ILLUSTRATION BY JOE ZEFF DESIGN

chology has shifted over the past couple of years. Americans have not simply become less brand loyal. Buffeted by financial forces beyond their control, they are ornery and disinclined to trust corporations—especially those that make lavish promises. Ford has momentum, but its success is a recent phenomenon. The company still needs to prove itself. "We're very suspicious, our confidence is shaky, we're not feeling very good," says Faith Popcorn of the marketing consultancy BrainReserve. And GM will have to tread especially carefully. American taxpayers won't soon forget that the U.S. government bailed out the company, a policy that proved to be very unpopular even though it saved thousands of manufacturing jobs.

It's not as though Detroit has the highway to itself. Honda, Nissan, Hyundai, Kia, and others could also pick up new customers. That's why GM and Ford can probably forget about making a patriotic appeal to "buy American." Buyers arrive at dealerships armed with detailed pricing data they found on the Web, and if Hyundai has the best combination of features and price, they'll drive a Hyundai. "Americans are forward-looking," says Nancy Koehn, who teaches history at Harvard Business School. "Instead of waving an American flag, I could see Ed Whitacre walking through the plant, passing a mechanic, saying, 'We've made some mistakes, we've learned from the past, but here's how we're getting better, working on making America strong.'" Koehn says Americans like feeling they're helping the country progress, not just boosting U.S. companies.

As Whitacre and Mulally have surely not forgotten, Toyota

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Kicking the tires at a Ford dealership at the Thousand Oaks (Calif.) Auto Mall

remains a force. No one can argue that the company handled its recall crisis with aplomb. And given its internal problems—overexpansion has stretched its resources—the odds of it stumbling again are high. But once Toyota gets past the current round of recalls, it can be counted upon to rev up its marketing machine. The company has done a remarkable job in recent years of embedding itself in the American culture. Toyota employs nearly 40,000 Americans in six states, mostly in the South, and as it has proven for 40 years, it knows how to make cars that Americans want to buy. Spokesman John Hanson says the carmaker can win back confidence by handling the recall well and fixing its quality problems.

The comeback campaign has already begun. During the Super Bowl, Toyota aired a commercial that waxed nostalgic about its long years of manufacturing reliable cars in America. It's the kind of pitch that appeals to loyal customers like Brian Yamashita, 47, who works in tech support in Orange, Calif., a Toyota stronghold. He just plunked down $17,000 to buy a 2010 Corolla. Before that, he drove a '98 Tacoma pickup for 238,000 miles. His mother drives a Lexus. He figures the Japanese automaker will figure out its quality issues and his car will be fine. Would he buy another? Absolutely. "I have faith Toyota will get it resolved," Yamashita says. "With any industry, whether it's cars, hamburgers, or spinach, there will be problems. I could do a lot worse with other manufacturers."

In other words, Detroit's window of opportunity won't stay open for long. "If you're going to grab market share from Toyota," says *Consumer Reports'* Champion, "you have to do it in the next nine months." GM and Ford can't count on Toyota to keep kicking the ball into its own goal. They will have to convince people their cars are worth buying because they are sharply designed, reliable, and fun to drive. If they do that, they might just find a way to turn one big break into a streak of good luck. | BW |

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Toyota on the Potomac

As the Japanese automaker hustles to complete an orderly recall of millions of vehicles, it is mounting an image-restoring counteroffensive. In Washington, reports Politico.com, the company is ramping up its already considerable lobbying operation in an attempt to head off a political backlash. Politico cites Senate records showing that "Toyota-related entities spent $4.1 million on lobbying last year—and $35.2 million during the past decade."

To read the story, visit **http://bx.businessweek.com/toyota-motor-corp/reference/**

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"I'm convinced that new finds in natural gas are going to produce a significant amount of fuel switching in the United States and there will be very significant [greenhouse gas] reductions." [1]

- Senator John Kerry
December 17, 2009 – Copenhagen

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Natural gas can cut our nation's CO_2 emissions from power generation in half. Today. Most alternative energy sources need time and money. Natural gas just needs you. Help us make American natural gas a central part of the country's plans for energy and climate security. Contact your elected representatives and, to learn more about our work, please visit CleanSkies.org.

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[1] Press conference on U.S. climate change proposals at Bella Center, Copenhagen, Denmark, December 17, 2009. Video recording of Sen. Kerry's full statement on file at American Clean Skies Foundation.

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A CARIBBEAN TAX HOLIDAY

The IRS is investigating how $100 billion a year in retail credit-card receipts is escaping taxation

By Jessica Silver-Greenberg

Illustration by Matt Dorfman

Greg Hennessy designs software in New York, where his $2 million-a-year company, SWAT, is based. His customer credit-card payments go to a bank in Panama, where his business is incorporated. As a result, he pays taxes at Panama's bargain-basement rates, far lower than what he'd owe in the U.S. "So far," he says, "it's been excellent."

Red Ball, a company in Phoenix, runs Web sites selling collectibles, software, and assorted other goods. It routes its nearly $15 million in card revenue to the tropical island of Nevis, where Red Ball is incorporated. Gregg Larry, who heads the company, says: "Sure, we get to pay less income tax, but it's not about tax evasion."

These two tiny companies illustrate a growing trend. At a time when the Obama Administration is preparing for a bitter battle with big multinationals over closing arcane tax loopholes, legions of mostly small retailers and service providers are minimizing their U.S. tax bills by sending credit-card receipts to Panama, Nevis, Aruba, the Cayman Islands, and other business-friendly havens. The IRS estimates that $100 billion a year in revenue is escaping U.S. sales and income taxes in this manner.



Private equity firm KKR brought in former Compaq CEO Capellas to run First Data

RAY NG

For several years the tax agency has been formally investigating whether the spreading credit-card practice amounts to illegal behavior. Daniel Reeves, the IRS special agent leading the probe, said in April in an affidavit filed in federal court in Denver that "a number of U.S. taxpayers may be under-reporting income, evading taxes, and breaking the law" by sending card receipts offshore. Reeves declined to talk to *Bloomberg BusinessWeek*, and the IRS won't provide specifics about the continuing probe.

Companies that route card revenue offshore say what they do is entirely lawful and appropriate. They typically note that they do not have to charge their customers any American sales tax because they have incorporated overseas. The companies say that they notify the IRS of this arrangement. They also maintain that eventually they pay income tax on

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any money they bring back to the U.S. Tax experts say that if businesses take all of these steps, they are indeed operating within the law.

The IRS suspects that a lot of the offshore credit-card activity isn't, in fact, reported and that repatriated funds frequently escape income taxation. Some executives in the business of processing card payments in the U.S. agree. "You can report a foreign bank account all day long, and that doesn't mean that you are accurately reporting the amount of money stashed there," says Todd Fuller, senior vice-president of Jetpay Merchant Services, a domestic U.S. card processor that competes against companies that arrange for offshore deposits.

Many Caribbean locales levy little or no sales tax, compared with state tax rates of up to 10% in the U.S. Similarly, many Caribbean jurisdictions impose corporate income tax rates far below the standard U.S. rate of 35%.

Hennessy, the software designer, says that while he benefits from this discrepancy, he nevertheless follows the rules. "I comply with all tax laws," he says. "I prefer to have my bank account in Panama, where it's safer than in the U.S., at least from frivolous lawsuits." Red Ball's Larry said he got fed up with paying high processing fees at home: "I just got sick of it." It's cheaper to send receipts to Nevis, he adds.



Carillo says he helps set up about 20 offshore accounts a day for U.S. businesses

PHOTOGRAPH BY JOSH RITCHIE; MAP BY STANFORD KAY

The credit-card investigation is unfolding as the Obama Administration cracks down on a variety of corporate and individual tax-minimization strategies. In the best known case, the U.S. government has pressured the Swiss banking giant UBS to turn over the names of 4,450 American clients who the IRS suspects are using offshore bank accounts to shield personal wealth from income tax (page 26). UBS avoided criminal prosecution in the U.S. by agreeing to pay a settlement of $780 million and admitting it helped foster tax evasion.

In the offshore credit-card probe, the IRS is looking into international payment processors that help U.S.-based businesses export their card receipts, according to people familiar with the investigation. The largest such processor is First Data, which operates from offices in Shady Springs, Ga. The private equity firm Kohlberg Kravis Roberts purchased First Data for $26.4 billion in 2007 and installed as CEO Michael Capellas, the former chief executive of the computer company Compaq. Capellas declined to be interviewed.

Last April the IRS issued a subpoena to First Data, demanding the names of all U.S. merchants that have retained the company to help them deposit credit-card receipts in foreign banks. The IRS has not accused First Data of any wrongdoing.

First Data, which employs 25,000 people worldwide, says it has complied with the IRS subpoena. The company rejects any suggestion that it facilitates tax evasion. "First Data does not support or approve any practice that violates United States tax law, including the transfer of credit card proceeds by United States businesses to offshore accounts for the purpose of unlawful tax avoidance," it said in a written statement circulated last year in response to the IRS subpoena. Spokeswoman Elizabeth Grice said in an e-mail response to questions from *Bloomberg BusinessWeek* that the company's international services are intended only

$100 billion

Company revenue that annually goes untaxed in the U.S. because of offshore credit-card processing.

Data: IRS

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for corporate customers based outside the U.S. None of First Data's customers has been accused of impropriety in their dealings with the processor.

In contrast to First Data's current statements, some past online advertisements circulated by company subsidiaries and affiliates seemed to invite U.S.-based retailers to transmit card payments offshore. A wholly owned First Data unit, CardService International, has promoted a service called "split-jurisdictional settlement." That term refers to the practice of depositing a portion of credit-card receipts in U.S. bank accounts and another portion in non-U.S. accounts. In a 2001 press release, First Data itself said it helped "U.S. merchants to settle domestic credit card transactions in the United States, but have payments with universally accepted cards, such as MasterCard and Visa, settled to international jurisdictions."

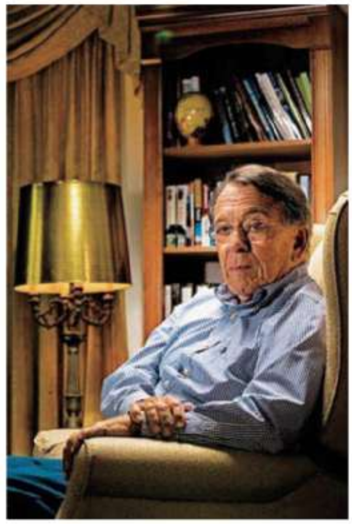
More recent First Data promotions don't address helping American businesses process payments abroad. "The people involved with those specific [earlier] promotions are no longer with the company," says First Data's in-house managing attorney, Ralph Shalom.

Filings in two court cases suggest that First Data has helped route receipts from U.S.-based businesses to overseas tax havens. A 2006 lawsuit filed in U.S. District Court in Miami concerned a contract dispute between Republic Bank Ltd., a Trinidadian institution, and Optimal Payments, a Canadian card processor. Optimal stated in court papers that First Data helped transfer credit-card receipts for some of Optimal's business clients to the bank in Trinidad. A separate 2003 suit in U.S. District Court in San Francisco involved a contract dispute between two American companies: Payment Resources International and Paycom. In that case, Paycom said First Data deposited credit-card receipts from U.S. businesses associated with Paycom into Banco Uno, a Panamanian bank. Both suits have been dismissed.

Asked about these court filings, First Data's senior vice-president for communications, Chip Swearngan, says the company conducted itself lawfully and ethically. "We can assert from looking at these cases that First Data did not settle accounts for U.S. merchants offshore," he adds.

The IRS offshore card investigation evolved from narrower probes of the tax-haven activities of online pornography and gambling businesses, according to people familiar with the situation. One of the initial targets, Internet gaming company Bet on Sports, shut down in 2006 after the IRS alleged it illegally solicited bets from American citizens and routed payments to offshore bank accounts.

FriendFinder Networks, based in Boca Raton, Fla., runs dating Web sites, including some that appear to promote casual sex. Assembled from components of the adult entertainment company Penthouse Media Group, FriendFinder reported $224 million in revenue for the first nine months of 2009. The company processes the bulk of its credit-card revenue through a subsidiary in tropical St. Kitts, a low-tax jurisdiction, according to filings with the Securities & Exchange Commission. FriendFinder CEO Marc H. Bell declined to comment.



RICHARD FREEDA/AURORA

Bauman says taxes are the only reason to deposit card receipts in a low-tax locale

Now, more mainstream businesses are exploring sending card receipts abroad, according to card-processing experts. Charles Carillo says he spends 70% of his workday as a manager at the processor Offshore Merchants arranging IRS-compliant foreign accounts for U.S.-based businesses. These range from travel agents to loan modification companies to online vitamin marketers. He won't name his clients. "On average, we set up about 20 accounts a day for U.S. businesses," Carillo says.

Some American businesses say that because domestic banks view them as too risky, their only feasible option is to process card receipts abroad. "A lot of businesses—like ticket sales, or gym membership providers—can't get a U.S. merchant account," says Peter McFarlane, who writes a financial newsletter called *The Q Wealth Report*. "Regardless of their individual financials, they are deemed way too prone to charge-backs," meaning customers who cancel orders. Banks generally don't like doing business with smaller companies that have high rates of cancellation.

Others familiar with card processing say taxes almost always figure into the decision to go offshore. Robert Bauman, a former Republican member of the U.S. House of Representatives from Maryland, works with Sovereign Society, an asset protection company in Delray Beach, Fla. Apart from avoiding the attention of the IRS, he says, "There is simply no reason that a U.S. business needs to have card proceeds deposited in a low-tax locale." | BW |

Business Exchange

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Less Taxing Places to Retire

The Daily Telegraph offered a different perspective on offshore tax havens in a Feb. 10 dispatch. The British paper suggested that retirees "may like to look further afield from the usual countries to get the best tax breaks and income tax rates." Monaco and Andorra, for example, offer a sense of romance, and neither country has taxes on income, inheritance, or wealth, the newspaper noted.

To read the full article from the Telegraph, go to **http://bx.businessweek.com/tax-reduction/reference/**

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GOODBYE, IRELAND

A JOB FAMINE FORCES A NEW GENERATION TO HEAD OVERSEAS

By Kerry Capell

Photograph by Jude Edginton



DUBLIN

When Simon Phelan started a civil engineering degree at Dublin's Trinity College four years ago, he figured his biggest problem upon graduation would be deciding which job to choose. Ireland's economy was growing at 5.4%, unemployment was a mere 4.4%, and construction was booming.

Today, with graduation fast approaching, only two of Phelan's 100 classmates have even had interviews. Worse, in these recession-scarred times, just two people from the class ahead of him are employed. So Phelan and many contemporaries see emigration as the only option. "The lack of jobs is driving people away," the 20-year-old Dubliner says after trawling through the meager offerings at Trinity's career office, a small building tucked off the school's cobblestoned quadrangle. "Ireland will lose a whole generation of graduates."

It's a scenario most Irish thought had gone the way of the potato famine and two-shilling pints of Guinness. Two decades of prosperity had transformed the island nation of 4.5 million from a European laggard into the so-called Celtic Tiger. After a century and a half in which Ireland's young and energetic routinely fled to South Boston or London's Kilburn, today's twentysomethings grew up expecting to live and work at home. But with one in three males under age 25 out of work, their confidence seems to have been misplaced. "It used to be employers were fighting over graduates," says Shane King, a 22-year-old Trinity senior from County Mayo on Ireland's west coast. "Now graduates are fighting each other for jobs."

The country's budget swung from a surplus in 2007 to a deficit of nearly 12% of gross domestic product last year as the economy shrank by 7.5%. A decade-long property bubble, which saw real estate prices triple, led to a banking crisis that Standard & Poor's estimates could cost taxpayers as much as

REDUX

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"The lack of jobs is driving people away," says Trinity College senior Simon Phelan

$34 billion. "Everything we have is being spent on the banks," says David Begg, head of the Irish Congress of Trade Unions.

Drive the 10 miles from central Dublin to Citywest, an industrial park near the border of County Kildare, and you'll see ample evidence of overbuilding. On the banks of the Liffey River, there's the half-finished shell of Anglo Irish Bank's new headquarters. Farther on, "for sale" signs dot posh developments where new homes stand unoccupied.

AUSTRALIA BOUND?

Many would-be emigrants have made the same trip. On a chilly Sunday, hundreds of people gather in a conference room at the Citywest Hotel for a seminar on emigrating Down Under. Representatives of several Aussie states sit behind foldable tables stacked with pamphlets extolling Australia's low unemployment and "no worries" outlook. Carpenter Michael McGerr, 38, drove more than 100 miles with his wife and toddler to attend. "Our goal is to go away for good," he says.

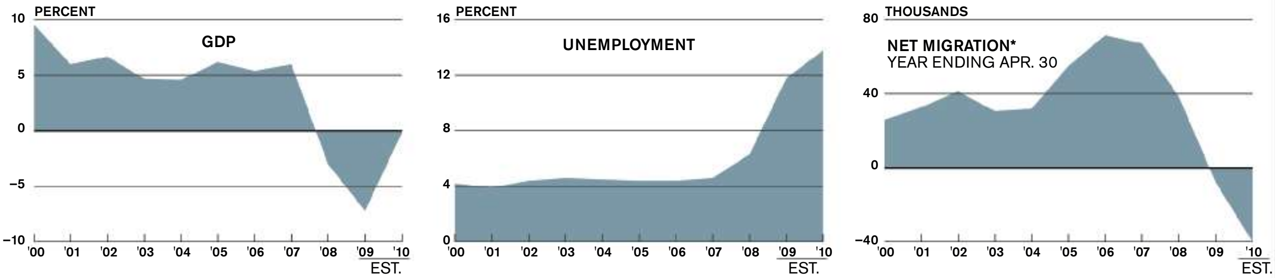
Last year emigration exceeded immigration for the first time in 15 years as 65,100 people left, outpacing arrivals by nearly 8,000. Almost half of those who decamped were recent immigrants from Eastern Europe. But with few opportunities at home, growing numbers of native Irish are also headed for the exit. "There was loads of work three years ago, then it just dried up," says Patrick Maye, an unemployed bricklayer who traveled to the Aussie seminar from Carlow, some 50 miles south of Dublin. The 22-year-old hopes to move to Australia once he finishes retraining as a fitness instructor.

With unemployment set to hit 13.8% this year, things are sure to get worse. The Economic & Social Research Institute (ESRI), an independent think tank in Dublin, predicts net outward migration of 40,000 for the year ending in April, the highest level

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THE CELTIC TIGER WHIMPERS

As Ireland's economic growth has slowed, unemployment has soared and more workers are leaving



Data: Central Statistics Office (Ireland); Economic & Social Research Institute

*Immigrants minus emigrants

in more than 20 years. "We are right back to the 1980s," says Piaras Mac Éinrí, a lecturer at University College Cork.

Back then, unemployment soared to 18% as the economy took a dive. Then in the 1990s, a wave of foreign investment swept Ireland, lured by low corporate taxes and inexpensive workers. Now the blue chips are scaling way back. In the past year, Intel, Royal Bank of Scotland, and Waterford Wedgwood have downsized; Dell moved PC production from Limerick to lower-wage Poland; and some 1,500 smaller companies have folded. Last year 170,000 Irish jobs vanished, and ESRI predicts 76,000 more will be lost in 2010.

One problem is that Ireland got too pricey. The American Chamber of Commerce Ireland estimates that from 2004 to 2008, Irish wages rose 50% faster than the average of advanced European economies. Former Intel Chairman Craig R. Barrett says that of the 14 reasons Intel came to Ireland two decades ago, only one remained: a low corporate tax rate of 12.5%. "Ireland needs a new game plan," he said at a Dublin conference in September.

In the past, the state has been a big creator of jobs by hiring civil servants and promoting investment. But to plug a yawning gap in public finances, Dublin in December announced spending cuts of $5.6 billion, including $1.4 billion from public sector pay and $1.1 billion from social welfare benefits. The tough measures have helped restore Ireland's standing among global investors, but the cuts make it difficult for the government to launch the policies that might enable people to ride out the recession, either in on-the-job training or higher education.

The biggest job casualties have been in construction. At its peak in 2007, the building trade employed 1 in 7 Irish workers. But over the past two years, the sector has shed 200,000 jobs, according to Ireland's Construction Industry Federation. "We went from being in high demand to no demand," says Gordon Cobbe, a construction manager from Cork. Out of work for a year, he plans on moving to Perth, Australia.



Some 170,000 Irish jobs vanished last year, putting pressure on food banks

Many Irish aiming to get out face problems similar to workers in, say, Detroit or Toledo: They can't afford to leave their homes. John McKenna is eager to join more than a dozen friends who have moved to Australia. With business slow at the plumbing supply store where he works, "I don't know how much longer I'll have a job," the 39-year-old says. But the house he bought for $306,000 in 2006 has halved in value, so it'll be tough to depart anytime soon.

The emigration surge comes as Dublin tries to implement a program called "Smart Economy." The plan is to boost innovation through tax breaks for research, expedited visa processing for skilled workers, a $689 million fund to back promising tech startups, and other incentives. The glue holding it all together, the government says, is "the knowledge, skills, and creativity" of the Irish—a problem with so many people leaving. "There is a risk that many of the talented individuals envisioned as the foundation of the innovation economy will make their careers elsewhere," says John McHale, an economics professor at the National University of Ireland, Galway.

Other economists are more optimistic. Alan Barrett, a research professor at ESRI, says the current exodus is likely to be benign. As part of the EU, Ireland will again lure immigrants from across Europe as growth picks up. And he points out that many who left in the '80s returned with better skills. "As soon as the economy recovered, people came back in droves," he says.

Kevin Carey, CEO of moving company Careline International, can attest to that. His firm helped relocate emigrants in the 1980s before bringing many back a decade later. Now most of his work is again outbound, and business was up 23% last year. His customers weren't so lucky. "They're all leaving; the cost of living here is too high," says Carey, who was manning a table at the Australian emigration event at the Citywest Hotel. For him, at least, business was good. | BW |

PHOTOGRAPH BY CATHAL McNAUGHTON/REUTERS; CHART BY ALBERTO MENA/BW

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LOVABLE LLOYD



What can we do to make normal Americans more properly appreciative of Goldman? A few ideas...

BY MICHAEL LEWIS

TO: Lloyd Blankfein
RE: Winning the Public Relations War

Our predicament is dire. Ordinary Americans wish to control not just our pay but our core values: We at Goldman Sachs have long stood for the right of every prop group to trade against its firm's customers. If we abdicate that right, who are we, deep down? In just the past few days many of us on the Goldman trading floor have wrestled with that question. We believe that rather than rethink our core values we should rethink our relations with the American public. Hence this memo. Your recent nonverbal signals—your habit of passing directly behind my trading desk en route to the elevators, your selection of the urinal adjacent to my own—convince me that you value my thoughts. As it happens, I have recently conducted a thorough study of the culture of mortals—or, as you refer to them, "The Morts." Please take the following ideas in the spirit in which they are intended: a team spirit. There is no "I" in Goldman Sachs, or in me. Nor will there ever be.

GIVE THE MORTS A SMALL, PERHAPS EVEN ILLUSORY, STAKE IN OUR UPSIDE. We have all seen the effects on the hearts and minds of our government officials and business leaders when they sense that our prosperity might one day be theirs. In the past year Warren Buffett has gone from being a leading critic of Wall Street to the greatest defender of Wall Street bailouts. Him we needed to pay hard cash—most accept less. That's perhaps the most curious trait of these ordinary Americans: You don't need to give them any money to lead them to hope that you might. Take Larry Summers, for instance. We both know that we would never actually employ even this surprisingly intelligent Mort in anything but the most humiliatingly ceremonial role. But he doesn't know that—and thus he has done so much for us.

Obviously, we can never employ large numbers of ordinary Americans. But if you stop for a moment and think like a Mort you will realize that we don't need to. We need only harness two more of his many irrational traits: overconfidence, plus a willingness to ignore the odds—as evidenced by everything from his interest in the Lotto to his belief in what he calls "love."

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Each year, for example, Goldman Sachs might announce a grand national competition, much like "American Idol." Finalists will appear before a national television audience to be judged by a panel of three rather ordinary looking Goldman executives. On stage they will perform various Wall Street tricks: negotiating with Tim Geithner, lobbying the Senate Banking Committee, designing securities that blow up, selling bonds to Germans, etc. The winner receives a job at Goldman Sachs. Which brings me to...

GIVE MORTS THE ILLUSION THAT THEY HAVE BEEN ADMITTED INTO OUR REALM, AND CAN NOW TRULY SEE WHO WE ARE AND WHAT WE DO.
The winner of our national competition, for instance, might easily be attached to a small Web-enabled, head-top photographic device. Thus equipped he would become the eyes and ears of Morts everywhere. As he stumbles around our offices, attempting to understand that which is beyond his comprehension, he will no doubt create what ordinary Americans refer to as "comedy." Morts love to laugh, to the point where they interpret our most straightforward remarks as occasions for humor. As we do not respond to comedy, it will not disrupt the flow of our business, and we can encourage it.

Let me say here that I, like every other Goldman trader, have admired the lengths to which you have gone to resemble an ordinary, nonthreatening American. Your conscious decision to forgo muscle definition, along with your persistent hairlessness, has been nothing less than enlightened public relations.

But there is only so much one human being can do, even when that being is more than human. Our employees along this new interface with Mort culture should reinforce your subliminal message. They should be "normal looking" and trained to mimic the Mort's strange, emotional responses to external stimuli.

But the main purpose of any new personal contact with individual Morts is to address what is perhaps our biggest problem: the new belief of ordinary Americans that they now, finally, understand what we do. That our work should be as simple as "facilitating productive enterprise," or "allocating capital." They have lost their former awe; we must restore it. Notice that they do not begrudge professional basketball players their vast salaries: They can see that those players are so unlike themselves as to constitute a different species. As our differences lie below the surface, they are harder for the Morts to perceive. Closer proximity to us, and our complexity, will solve this problem. They will soon weary of trying to comprehend what we do and go looking for another outlet for their personal frustrations. Which brings me to my final thought...

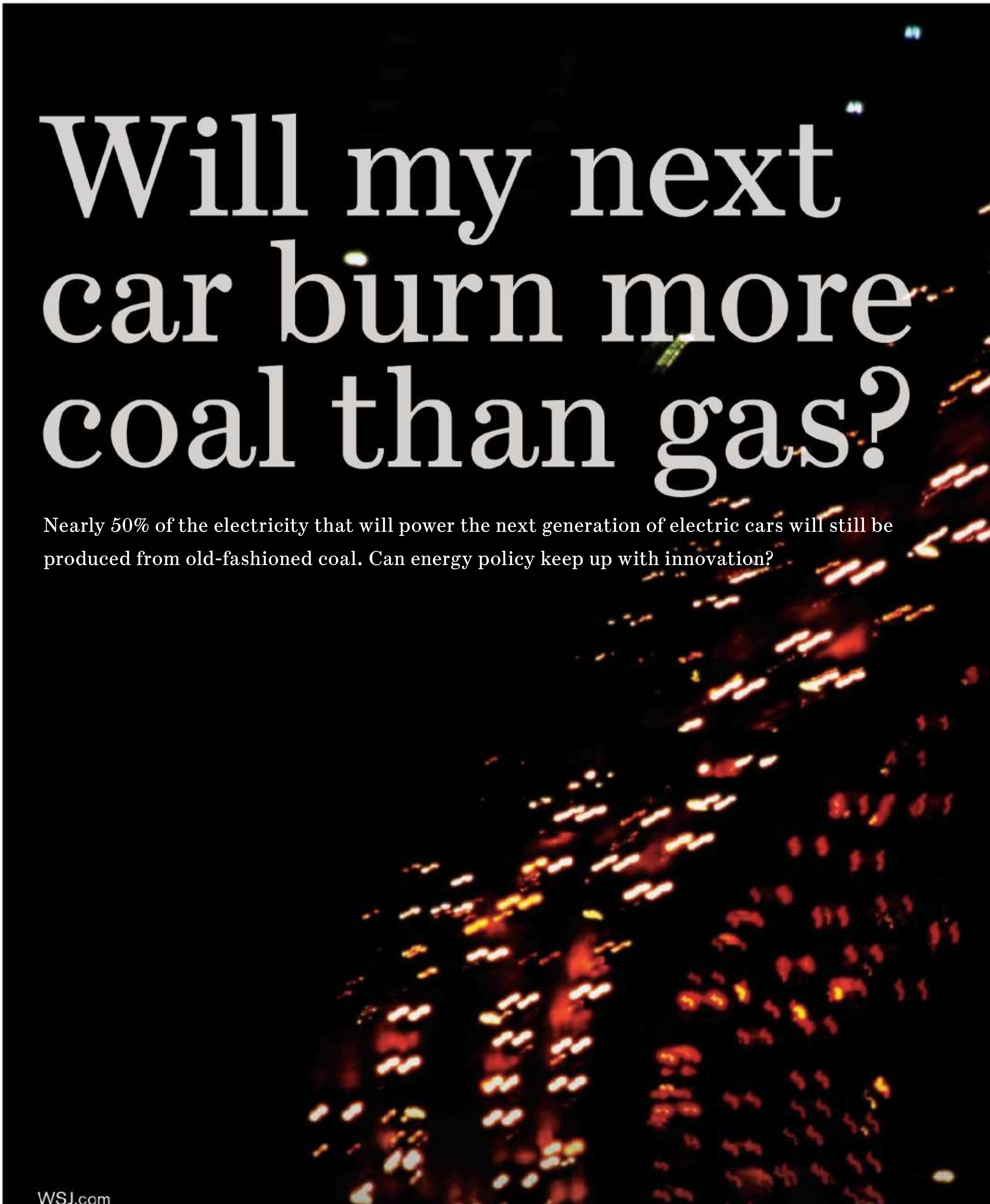
REMIND THE MORTS OF THEIR MORE NATURAL RESENTMENTS.
At the moment they mistrust us, perhaps even despise us, but their feelings toward us are new and thus shallow. They have had 30 years of training in hating their own government (the ultimate example of Mort irrationality). We must remind Morts that we share a common enemy: them.

Michael Lewis, a columnist for Bloomberg News, *is the author of* Liar's Poker, Moneyball *and* The Blind Side. *His next book,* The Big Short, *will be published in March.*

MELISSA GOLDEN/REDUX (BLANKFEIN); DAVID RUDES/BW (STILLS)

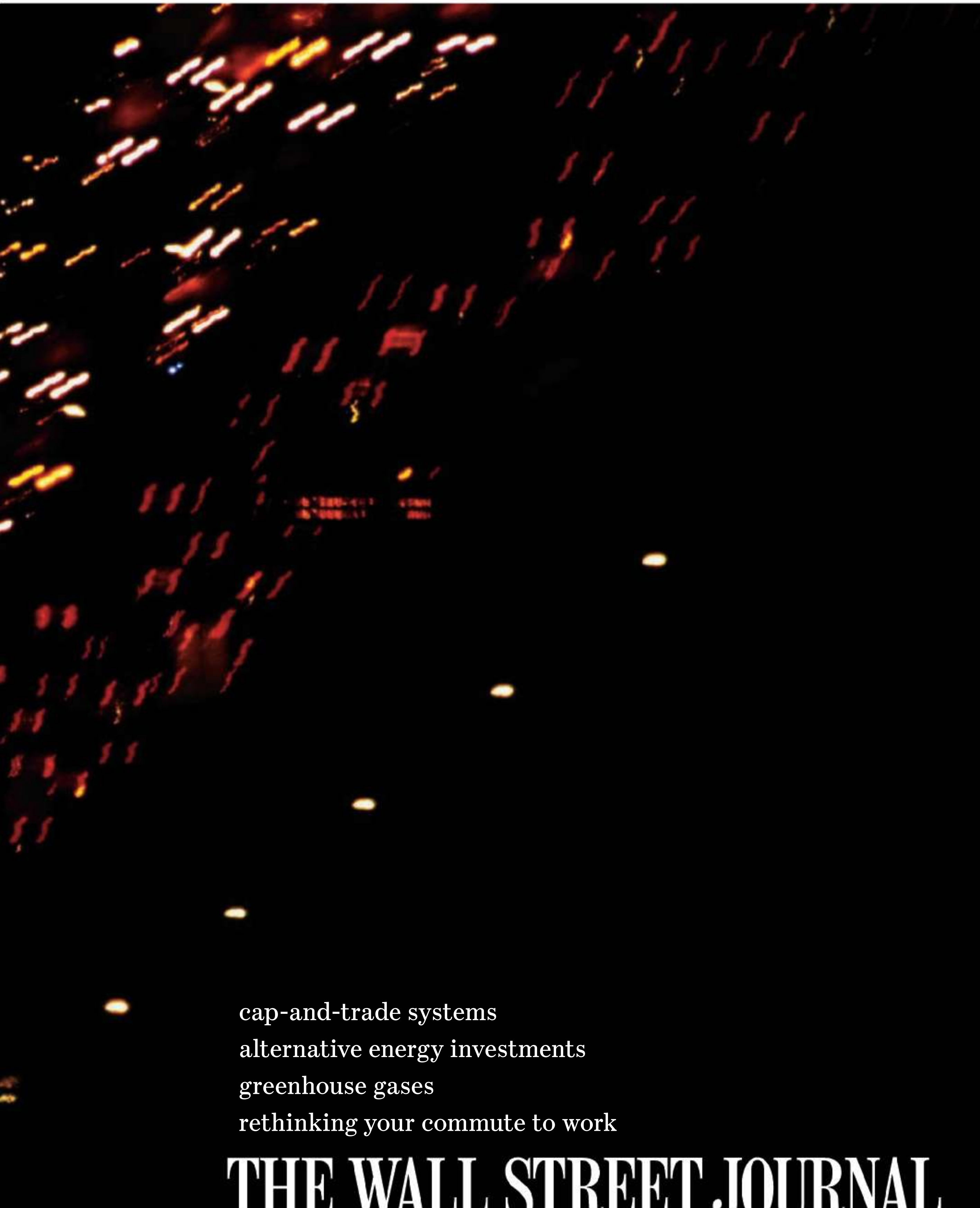
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Excellence in Energy



Eleven years ago Platts established the Global Energy Awards to showcase extraordinary accomplishments by energy businesses and individuals worldwide. The Awards recognize excellence and innovation by companies and executives throughout the global energy industry. A total of approximately 150 individuals and companies were finalists for the Platts Global Energy Awards in 2009, with hundreds more nominated.

Platts receives a growing number of nominations each year, with nominations coming in from more than 20 countries in 2009, including Brazil, India, Puerto Rico, Saudi Arabia, South Africa, Spain, Russia, Switzerland, Argentina, China, Pakistan, Bangladesh, Thailand, the United Kingdom and the United States. The Awards bring together peers from around the world to honor a select group of pacesetters. The Platts Global Energy Awards have been described by past entrants and winners as both the "World Series" and "Academy Awards" of energy.

platts GLOBALENERGYAWARDS 2009

In 2009 the Awards recognized excellence and innovation by companies and executives in more than a dozen categories within the global energy industry. As we enter into the second decade of this century, the next ten years appear poised to be as tumultuous as the previous ten. Accordingly the energy industry is transforming itself to meet the challenges of the 21st century and beyond, while honoring the achievements of those who have excelled in the present.

Awarding excellence once a year has become the industry's way of acknowledging struggle, saluting innovation, and celebrating success.

Renewal and Responsibility

As the world economy begins to emerge from the economic volatility of the past two years, energy is expected to again be in the spotlight. If finance lubricates the world economy, then energy is its fuel. The machine that is global growth runs on what the global energy industry mines, pumps and generates.

It is true that an industry as pervasive and vital as the energy industry gains a degree of importance to society that most other industries do not. But with power—be it of the fossil, solar or grid kind – comes responsibility, and the global energy players have been working to not only find their own way through price volatility, geopolitical crises and changing political climates, but to continue to deliver their product to the billions of people around the planet to whom it is critical.

The future is unclear, and context is key. The world has just gone through the worst economic slump since the Second World War, and while there are indeed signs of recovery, no one knows quite when it will arrive. Many issues remain.

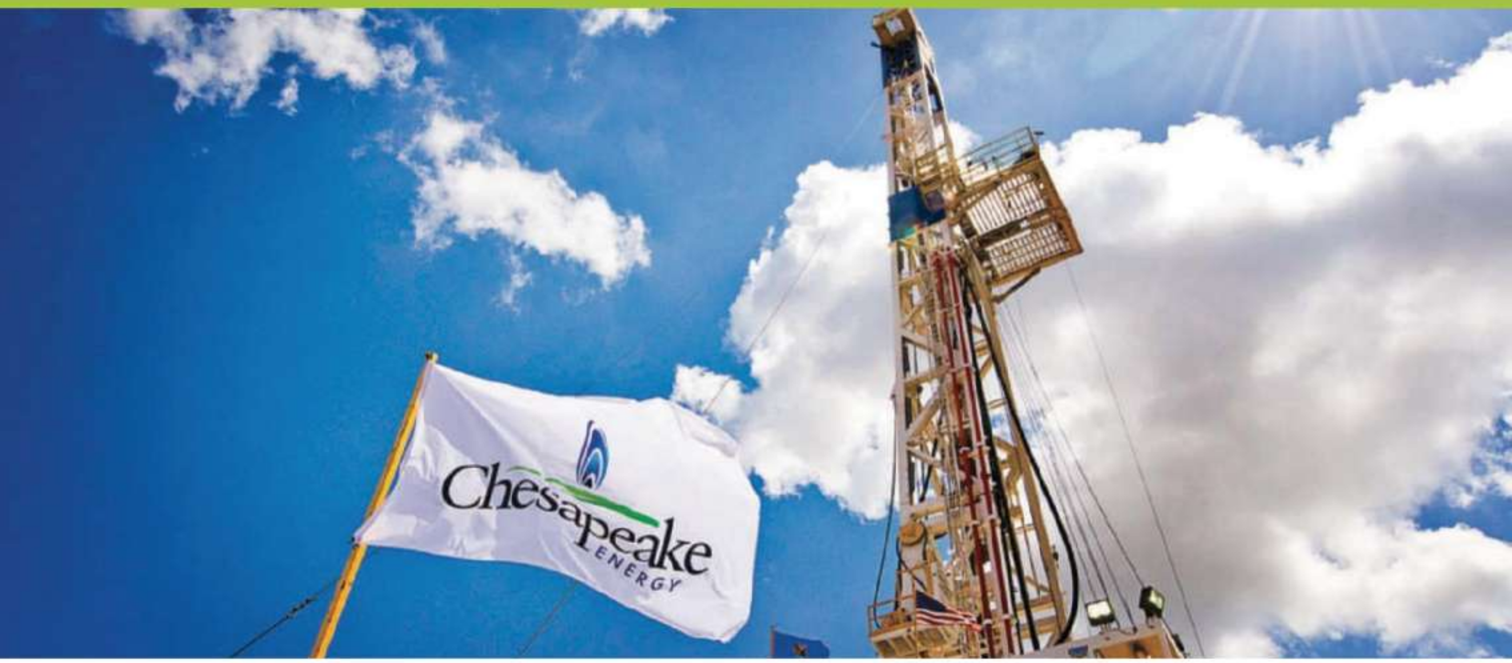
For those companies working in the petroleum sector, the last few years have seen an oil price collapse and then a rebound, with rising marginal costs pointing to higher prices in the longer term, but with experts wondering if current levels are sustainable. There's also been a slump in energy investment due to the financial crisis. The question of whether energy investment will bounce back quickly enough to avert a supply squeeze down the road is still on many industry minds. And finally, there is the issue of climate change, with a series of difficult negotiations on a post-2012 climate deal leading up to Copenhagen, which in itself produced mixed messages at best. The world still asks what is needed to do business in an era of climate change dynamics.

Demanding Growth

While global energy use fell in 2009 — for the first time since 1981 —the International Energy Agency (IEA) predicts that demand is set to resume its long-term upward trend once the economic recovery gathers pace. By 2030, the IEA predicts world primary

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Chesapeake is proud to be the nation's leading proponent for the greater use of U.S. natural gas. After all, in today's rapidly changing world, nearly everyone acknowledges the need for energy solutions that are clean, affordable, abundant and American. We're pleased to be featured in this issue saluting the Platts Top 250 Global Energy Companies & Global Energy Awards. As winners of the 2009 "Industry Leadership" and "Energy Producer of the Year" honors, we join *BusinessWeek* in celebrating our industry's best as we champion a cleaner energy future through the greater use of natural gas. **chk.com**

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energy demand as being 40% higher than in 2007. From 2007 to 2030, the agency sees fossil fuels remaining the dominant sources of energy worldwide, accounting for 77% of the demand increase, and electricity demand growing by 76%. If correct, that increase will require 4,800 gigawatts (GW) of added production capacity, almost five times the existing capacity of the United States today.

Upstream to downstream, delivering energy to the world has never been easy.

Yet in year 2030, 1.3 billion people will still lack basic access to electricity. Though that number is an improvement over the 1.5 billion people without energy today, it is still considered by most to be unacceptable. Universal electricity access could however be achieved with additional power-sector investment of $35 billion per year from now until 2030, and with only a modest increase in primary energy demand and related CO_2 emissions, but the outlook remains uncertain for those still residing in energy poverty.

Clearly challenges remain, but the energy industry has historically been buffeted by geopolitics, market forces, the environment and technological innovation. But the executives who lead today's energy firms on a daily basis know that turbulence is nothing new. Challenge is a constant in the energy industry, and while for some it would seem that the dynamics are a danger, veteran industry players know that it is about attacking problems head on, not retreat. From upstream to downstream, delivering energy to the world has never been easy. If it were, anyone could do it.

Winning Achievements

Platts Global Energy Awards judges chose Chesapeake Energy as Energy Producer of the Year for 2009. Chesapeake also received the Industry Leadership Award. This is the second time in three years that Chesapeake has been named the Energy Producer of the Year by Platts Awards judges.

The Energy Producer of the Year Award recognizes excellence in the upstream energy sector for companies that have set world-class standards in exploring for and finding new resources, maximizing technical excellence and innovation in resource extraction, and bringing complex or difficult projects to completion on schedule and on budget. The panel of independent international judges noted Chesapeake's expertise in shale gas and its very high success rate in exploration activities.

Aubrey K. McClendon, Chesapeake's Chief Executive Officer, commented, "We are proud of the accomplishments of our 8,300 employees and honored to be selected as the Energy Producer of the Year for two of the last three years."

The global nature of the energy industry was clearly evident in 2009, with companies from around the world recognized for their



The Winners of the 11th Annual Platts Global Energy Awards

CEO of the Year
James Hackett
Anadarko Petroleum Corporation (USA)

Commercial Technology of the Year
Repsol (Spain) - Kaleidoscope Project

Community Development Program of the Year
PTT Public Company Limited (Thailand)

Deal of the Year
Enel SpA (Italy) - Endesa Acquisition

Downstream Operation of the Year
S-OIL Corporation (South Korea)

Energy Company of the Year
Anadarko Petroleum Corporation (USA)

Energy Efficiency Program of the Year - Consumer
Johnson & Johnson (USA)

Energy Efficiency Program of the Year - Supplier
Pacific Gas and Electric Company (USA)

Energy Producer of the Year
Chesapeake Energy Corporation (USA)

Engineering Project of the Year
Mirant Corporation (USA)—Potomac River Generating Station Virtual Stack

ENR Energy Construction Project of the Year
Shell Exploration & Production - Perdido

Green Energy Initiative of the Year
Naval Facilities Engineering Command (USA) - Energy and Water Management Program for the Department of the Navy

Industry Leadership Award
Chesapeake Energy Corporation (USA)

Infrastructure Project of the Year
Entergy Corporation (USA) -
New Orleans Underground Natural Gas Service Infrastructure

Lifetime Achievement Award
Tom Casten
Recycled Energy Development

Lee Raymond
Exxon Mobil Corporation (retired)

Marketing Campaign of the Year
Peabody Energy (USA) -
"Coal Can Do That" Campaign

Power Company of the Year
FPL Group (USA)

Rising Star Award
Enzen Global Solutions Private Limited (India)

Sustainable Technology Innovation of the Year
Energy Storage & Power (USA)/PSEG -
Energy Storage Technology

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work. One in particular, Repsol of Spain, was given the award for Commercial Technology of the Year. Repsol's Kaleidoscope Project—a partnership of geophysicists, computer scientists and organizations worldwide for processing seismic data—has developed advanced computerized techniques that reveal previously invisible oil and gas deposits efficiently and cost-effectively.

Other global winners included S-Oil Corporation of South Korea for the Downstream Operation of the Year award; and Enzen Global Solutions Private Limited (India), which was given the Rising Star Award. The award for Deal of the Year went to Enel SpA of Italy for the company's Endesa acquisition.

PTT Public Company Limited or PTT of Thailand won the award for Community Development Program of the Year which its main purpose is to develop a role model of community development of self-reliant districts. PTT is a fully integrated petroleum and petrochemical company that operates as PTT Group whose operations ranging from natural gas, oil marketing and trading, to plastic pallet production. PTT Group is noted for its sustained growth, which has given it the momentum to move forward with its goal of becoming Thailand's premier multinational energy company.

"Our sustainable growth comes from our success in balancing between business performance and the well-being of people. Each year we keep on working harder for Thailand's energy stability and the better living of Thai people," says Mr. Prasert Bunsumpun, PTT Group CEO & President.

Platts Global Energy Awards judges recognized Mr. Bunsumpun in 2008, when he was chosen to share the CEO of the Year award. Mr. Bunsumpun has set three strategic principles for the company, including the development of a high performance organization, good corporate governance, and a commitment to corporate social responsibility.

Energy efficiency has been a hot topic among industrialists and policy makers alike over the past year. Johnson & Johnson of the United States won Energy Efficiency Program of the Year, consumer, and Pacific Gas and Electric of California won for Energy Efficiency Program of the Year, supplier.

Mirant Corporation, also of the United States, won the 2009 Engineering Project of the Year award for its innovative approach to improving air quality at its Potomac River Generating Station in Alexandria, Virginia. Mirant conceived of a "virtual stack" to address limitations in the original design of the station which was constructed in the late 1940s.

The awards came full circle with Anadarko Petroleum winning a second award for Energy Company of the Year. Three years ago Anadarko acquired two major competitors, and the judges highlighted the transformation within the company since then and during the recent global economic crisis. They praised the company and its CEO James Hackett for successfully steering Anadarko through numerous divestitures, exceeding its production targets, restoring its balance sheet and maintaining its commitment to exploration, which paid off in one of the world's top 10 discoveries offshore Ghana.

WEBSITES TO WATCH



Chesapeake Energy: http://www.chk.com

Oracle: http://www.oracle.com

PTT: http://www.pttplc.com

Platts: http://www.platts.com

http://www.globalenergyawards.com

Without our cars and lights, it would be a much different world for us all.

Excellence by Association

The world's energy industry is as diverse as the mix of resources it transforms. Crude oil, coal, nuclear power, natural gas, hydroelectric and renewables all make up the inputs of a vast, energy transformation machine. The companies that first come to mind are those on the front line of operating that machine; the oil majors, natural gas producers, nuclear power plant developers and the rest.

What's often forgotten is the importance of companies whose contribution to the industry could be considered the lubricant that keeps the machine from seizing up. One of those companies is Oracle Corporation, the world's largest enterprise software company.

As citizens, regulators and customers demand a more sustainable energy future, Oracle has been helping utilities turn information into power. The company builds and integrates mission-critical and business applications on a world-leading technology foundation to help utilities consolidate and use information. "Gathering and analyzing more data about how we produce, move, and use energy uncovers new ways to slash waste and bolster efficiency," says Guerry Waters, vice president for utilities industry strategy at Oracle. "Utilities are using information to get more from existing resources and help customers use less."

Oracle's industry involvement has most recently included sponsorship of the Platts Global Energy Outlook Forum on Sustainability, at which leading economists and energy experts participated in a lively debate about the true economics of proposed sustainable solutions for future electric power and oil supply.

Positive Outlook

Platts Global Energy Awards and Platts Top 250 Global Energy Company Rankings™ show that energy professionals have become increasingly adept at transforming raw resources into the energy that enables modern civilization. Without our cars and lights, it would be a much different world for us all.

Regardless of how the future energy landscape takes shape, the next decade of Platts Global Energy Awards and Top 250 Rankings will reflect the great decisions, strategies and advancements that are sure to happen. ■

Written by Henry Gentenaar.

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PTT combines a huge portfolio of companies spanning the entire energy and petrochemical chain. We are Thailand's major operator of gas business from offshore platforms to distribution pipelines. Our strong growth and outstanding performance have been marked by a world ranking that continues to rise. In parallel with our business growth, we take part in sustaining the future of this country by taking care of society, community, and environment, and will continue to do so, relentlessly.

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66 Electronic Arts under assault
67 Europe's hedge fund fight
68 Why CFTC's Gensler worries Wall Street
70 Post-Rapture pet care
71 Tory Burch's global ambitions
72 The gold-plated boardroom

WHAT'S NEXT



PHOTO-ILLUSTRATION BY SEAN McCABE, PHOTOGRAPH BY RICHARD DREW/AP PHOTO

STRATEGY & COMPETITION

Tyco's Ed Breen: Let's Deal

After steadying the scandal-tainted company, he sees acquisitions as the key to growth—again

By Diane Brady

Last fall, Edward D. Breen, the chief executive of Tyco International, played the corporate chieftain version of *Deal or No Deal*. General Electric was selling its security division, and Tyco was among the likely bidders. The acquisition would have been Tyco's first big one since 2002, when the company nearly collapsed amid charges of executive fraud. Some investors worried that GE's eclectic mix of equipment-oriented assets wouldn't be a great fit for Tyco's service-focused business. "It would have been a stretch," says Deane M. Dray, an analyst at FBR Capital Markets. Breen, 54, opted for no deal. When United Technologies announced on Nov. 12 that it would buy GE Security for $1.8 billion, investors sent Tyco's stock up 3%.

Breen, however, was itching to buy a company. On Jan. 18, Tyco announced it was acquiring Brink's Home Security (now operating as Broadview Security) for $2 billion. One might have expected investors to flee on the news; instead, they cheered. Here Tyco was buying a debt-free company that could be plugged neatly into its business. Whereas the stocks of most acquiring companies fall after a merger announcement, Tyco's rose 2%. The lesson: Breen could buy, but he had to buy smart.

Eight years into one of the biggest corporate cleanup efforts in history, investors are still scrutinizing Tyco's every move. Breen has replaced the board, paid down debt, settled a huge shareholder suit, and broken the $41 billion-a-year conglomerate into three pieces. But for all of his turnaround cred, he doesn't yet enjoy the latitude given to other CEOs to pursue deals. "Tyco's history means it will always face a higher bar on acquisitions," says analyst Steven E. Winoker of Sanford C. Bernstein.

That may complicate things for Breen, who is beginning to view dealmaking as essential to Tyco's long-term growth strategy. "We're now at the point where we can supplement our growth with acquisitions," he says. "We're in three global businesses, and we're the world leader, but not by a lot. We have an opportunity to become a much larger player."

To get there, Breen has worked to rid Tyco of the taint of the Dennis Kozlowski era. Under Kozlowski, Tyco became a symbol of runaway corporate excess, from the $2.1 million birthday party for his wife in Sardinia—complete with an ice sculpture of Michelangelo's David urinating vodka—to Kozlowski's practically deal-a-day buying binge that created a $36 billion conglomerate with close to $30 billion in debt. Years later, Tyco can't seem to erase

Business Exchange

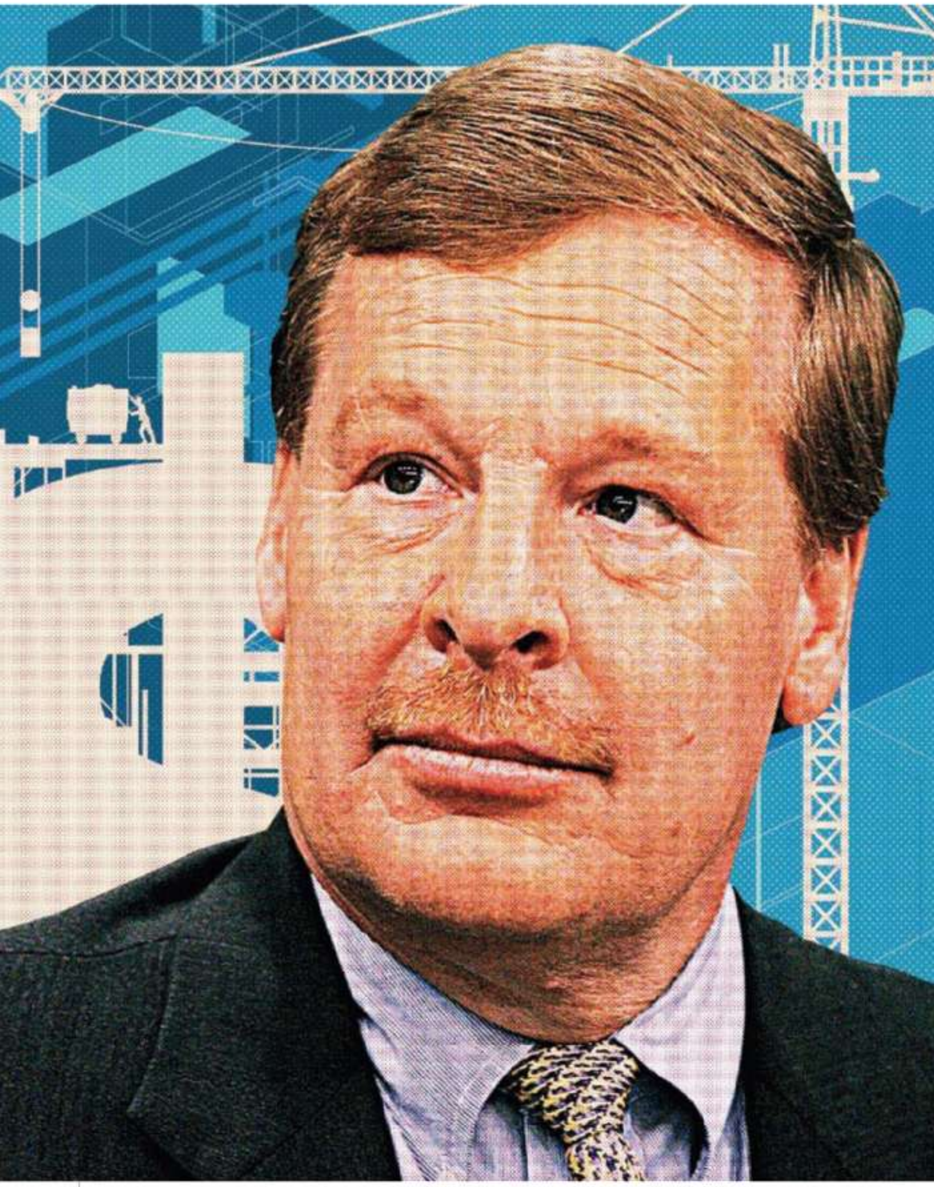
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The Brink's Job

According to SEC documents, Tyco chief Ed Breen approached Brink's Home Security Chairman Carl Sloane to suggest a deal on Jan. 20, 2009. The pitch didn't work. Eight months later he called again, and Sloane was all ears. What changed? GE was selling its security business, a move that may alter the competitive landscape.

For Tyco's S-4 filing, go to **http://bx.businessweek.com/mergers-and-acquisitions/reference/**

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Breen: Unlike predecessor Kozlowski, he approaches deals with caution

those memories. "There are still portfolio managers in some places who will not invest in Tyco because of the hurting they took," says Edward C. Arditte, Tyco's senior vice-president for strategy and investor relations. That's a big reason why Tyco still trades at a discount to rivals: Its stock fetches 13.5 times estimated 2010 earnings, compared with 16.8 for its peers, according to Bloomberg data.

Yet Breen and Kozlowski couldn't be more different. There's nothing inside Tyco's new Princeton (N.J.) operational headquarters to suggest that its CEO is celebrating his success. Breen can be seen eating in the corporate cafeteria or pouring himself coffee in a small pantry where someone has taped a sheet promoting an employee weight-loss challenge. He doesn't even have a parking space; often he has to walk across the lot. "The thing that offends me most is arrogance," says director R. David Yost, CEO of AmerisourceBergen. "Ed has none of that."

Breen spent much of his career in the cable industry. He led General Instrument, a maker of set-top boxes, before selling it to Motorola for $17 billion in 2000. He was president of Motorola, itself in the midst of a turnaround, when he suddenly quit in 2002 to rescue Tyco. "He said: 'If I can fix this, I could give something back to American business,' " recalls Frank M. Drendel, chairman and CEO of telecommunications company CommScope and a longtime mentor to Breen.

Breen walked in to find a company crippled by the scandal, massive debt—$11 billion of which was coming due—and an obsession with deals. "I banned the word 'acquisition' when I came," says Breen. "Tyco was acquisitions on steroids." Jim Spicer, president of Tyco's SimplexGrinnell fire protection business, is the only member of the senior team from the Kozlowski era. "What Ed has brought to the table is visibility, stability, vision, and a sense of purpose," he says.

SMALLER SANDBOX

In 2006, Breen broke up the company, spinning off Tyco Electronics—which makes electronic connectors—and health-care products unit Covidien, both of which had strong balance sheets. Breen kept what was left, a $17 billion business that includes security (ADT Worldwide and now Broadview), fire protection, and "flow control" (valves and such). "Not a lot of managers willingly make their sandbox smaller," says Tyco's Arditte. Soon after, friends and colleagues began to wonder whether Breen "would have the same interest in a smaller company," says lead director Bruce Gordon. "And he did. His ego is not wrapped up in revenues."

Despite Tyco's improved health, Breen has lately faced challenges. The financial crisis sent sales down 15% last year and prompted Breen to lay off about 7,000 of 113,000 employees. Analysts don't much like Tyco's $1.4 billion electrical and metal products business, because it is tied to volatile steel prices and commercial construction, adding a big gust of unpredictability to a company that now prides itself on stability. And given its history of ignominious acquisitions, the notion of Tyco jumping into a series of big deals may be off-putting to some. "You can imagine how skeptical people would be," says Winoker of Sanford C. Bernstein.

Breen is committed to converting investors, one deal at a time. "Every deal we do has to make sense strategically and financially," he says. "We've got a strong balance sheet, and I'm never going to let that change." BW

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EA's recent Mass Effect 2 war game has been a huge hit

STRATEGY & COMPETITION

Electronic Arts Under Assault

The leading maker of computer games is struggling as people turn to cheaper online alternatives

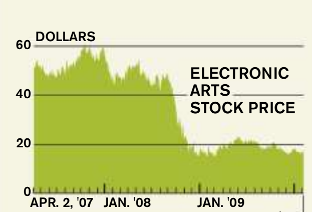
By Cliff Edwards and Adam Satariano

John Riccitiello saw the crisis coming. In August 2007, soon after becoming CEO of video game maker Electronic Arts, he gathered 160 lieutenants in New York and warned them that the $20 billion industry was headed for trouble. The major players were clinging to the model of selling shrinkwrapped games for $60 a pop, while users were turning to far cheaper online games. Only by "jumping into the abyss," he said, and radically changing itself could EA survive the looming shakeout.

The abyss proved to be deep. EA has lost money for 11 straight quarters since Riccitiello became CEO, and the stock is off 68% over the same period. The company has come up with lower-priced online games, but users have continued to flock to cheaper or free alternatives from upstart rivals. EA stunned Wall Street in January by slashing its outlook for the fiscal year ending in March, then again on Feb. 8 by providing a fiscal 2011 outlook that trailed some analysts' expectations. EA now expects to lose $197 million to $295 million for fiscal 2011 on sales of $3.45 billion to $3.7 billion, under standard accounting practices. "Management's credibility is nonexistent right now," says Patrick E. Becker Jr., chief investment officer of Portland (Ore.)-based Becker Capital Management, which holds about 1 million shares. (EA prefers to use nonstandard accounting that excludes certain charges, under which it expects to earn $165 million to $231 million for fiscal 2011.)

EA's SLIDE

The stock of Electronic Arts has dropped since John Riccitiello became chief executive



Data: Bloomberg

The question is whether EA and its boss will end up as casualties of the upheaval. Riccitiello, 50, doesn't sound defeated. EA, he says, has begun to roll out its strongest slate of games in years and supplement store sales with offerings for online and mobile phones. "You see a six-foot hole that we're in," he says. "I'm telling you that we were in a 20-foot hole and we've climbed 14 feet out of it."

VIRTUAL GOLF CLUBS

EA still gets about 80% of its revenues from traditional shrinkwrapped games, such as Madden NFL, the football tacklefest. But the company will make some major titles available online for free for the first time, beginning this year with four games including Tiger Woods Golf and FIFA Soccer. (Revenues will come from selling gamers virtual goods, such as digital golf clubs.) It's also preparing its most ambitious massive multiplayer online game, based on *Star Wars*, which will compete with the popular World of Warcraft beginning early next year. And EA may rework its Sims virtual world game to be played on social networking sites as an alternative to hits like FarmVille, from newcomer Zynga.

The trick—a considerable one—is to do all this without hastening the decline in traditional game revenue. EA's digital business brings in only $575 million now, and it's unclear whether Riccitiello can get it growing fast enough to replace losses in the traditional business. Investors may not have the patience for any more missteps. "[The earnings miss in January] was strike two," says analyst Michael Pachter of Wedbush Morgan Securities. "Shareholders will revolt if there's another strike."

CHART BY STANFORD KAY

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Riccitiello had been EA's president until 2004, when he left to found the private equity firm Elevation Partners with former Apple finance chief Fred Anderson and U2's Bono. At Elevation, Riccitiello studied the music industry's rocky transition away from compact discs and saw scary similarities in games. When he rejoined EA in April 2007, he worked out a two-year plan to manage the shift to digital. But the economic meltdown and increased frugality of gamers trashed it.



CEO Riccitiello: "We were in a 20-foot hole"

Riccitiello reworked his strategy last fall at a brainstorming session with his executive team. One major goal: Grab back some of the revenue EA and others were losing as consumers flocked to used games. The second-hand market now accounts for about a third of all games sold in the U.S., or $2 billion annually, says Pachter. At the meeting, Riccitiello green-lighted "Project Ten Dollar," a coupon program to reward people who purchase a new game with downloadable content and upgrades. People who buy used games pay an extra $10 or more for the same goodies. To create online products quickly, EA cut a deal in November to buy Playfish, which makes free games for social networks.

Still, the fundamental challenge remains. "While it's possible EA can make the extremely difficult transition from providing a shiny disc in boxes to [leading] in digital, history suggests it's rather unlikely," says Eric Goldberg, a managing director at Crossover Technologies who consulted for EA in the past.

Riccitiello contends EA can succeed in both boxed and digital games. In the traditional sphere, the company's new Mass Effect 2 war game sold more than 2 million copies in its first few days, and the new Madden product will redefine the way people play video football, he promises. Meanwhile, EA is making more games available on more devices than ever before, from game players like the Xbox to PCs and mobile devices like the iPhone. "We stumbled some," he admits. "The stumbling is gone, the execution is there." | BW |

PHOTOGRAPH BY ANDY FREEBERG; ILLUSTRATION BY DAVID POHL

FINANCE

Europe's Hedge Fund Fight

The EU says new rules will boost stability, but funds fear for their profits



By Mark Scott
LONDON

Many Europeans have a dim view of hedge funds and private equity firms, arguing that their speculative trading aggravated the recent financial turmoil. Now, European regulators are readying rules they say will help avert another meltdown—and hedge funds aren't happy about it.

Although the measures won't be final until summer, some version is likely to be approved by EU regulators. One proposal would cap borrowing, which might curtail leveraged buyouts and trading of complex financial instruments. Another would require fund managers to hold capital with third parties for safekeeping, which could force them to pay more for insurance. A third would bar managers outside Europe from marketing to investors in the region unless they submit to EU oversight. "If funds don't want to follow the rules, then good riddance," says Andreas Botsch, an adviser at the European Trade Union Confederation.

IMPACT ON THE RECOVERY

The financial industry worries that the plans would do serious damage to profits. European hedge funds oversee roughly $262 billion in assets, 16% of the global total, according to analytical firm Hedge Fund Research. The added oversight may cost hedge funds and private equity houses $4.5 billion in one-time costs, with an additional $434 million annually for compliance, estimates financial consultancy Charles River Associates.

Some economists say the proposals could harm the region's recovery, which already lags America's. EU researchers expect Europe's gross domestic product to expand a mere 0.7% this year, vs. 2.2% for the U.S. Advisory firm Europe Economics figures the rules would trim growth by 0.2 percentage points and boost unemployment. "I can't find a single investor who believes this is a good thing," says Douglas Shaw, a managing director in London for investment giant BlackRock.

Pension funds and other institutional investors, which often put money in hedge funds, are also unhappy about the idea. Ten Dutch pension funds say they'll lose a total of $2 billion in annual profit if the proposals are passed. "The [rules] could lead to an undue reduction of investment opportunities, higher costs, and lower returns for us," the group told the European Parliament in January.

With global competition for financial services intense, some say the regulations will spur managers to take their funds—and jobs—offshore. Poul Rasmussen, a former Danish Prime Minister and president of the Party of European Socialists who helped draft the proposals, counters that the new rules will protect jobs by clamping down on debt-fueled takeovers. Excessive borrowing, he says, "weakened firms, leading to an increase in corporate defaults during the crisis." | BW |

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Gensler is angering companies that use derivatives to hedge costs

ECONOMICS & POLICY

A Goldman Guy Turns on the Street

CFTC chief Gary Gensler's fight for tough rules on derivatives is making him exceedingly unloved

By Ian Katz and Robert Schmidt

Gary Gensler, chairman of the Commodity Futures Trading Commission (CFTC) and an ex-Goldman Sachs partner, has shattered any illusions that he will protect Wall Street from tough new derivative regulations. Over a private lunch at the Waldorf Astoria on Jan. 6, Gensler, 52, told executives from Credit Suisse, Deutsche Bank, Bank of New York Mellon, and Goldman that while he once shared their goals—to boost revenues and their own bonuses—his responsibility now was to taxpayers, according to people familiar with the meeting. When one banker asked Gensler what he saw as the biggest obstacle to reform, he gestured toward his hosts and replied: "You."

Of all the regulators in the Administration, Gensler may be the most troubling to the Street. He wants to drag derivative trading out of the shadows and expose to scrutiny the lush margins traders make on these complex securities. Companies use them to protect against oil price swings and other risks; sophisticated traders like to exploit them for profit. Gensler also wants to make it much easier for new competitors to enter the market, which would deprive the five U.S. banks that dominate derivative trading—Goldman, JPMorgan Chase, Bank of America, Morgan Stanley, and Citigroup—of billions in profit.

A House bill passed in December spells out new regulations for trading derivatives. Gensler thinks the bill should have been a lot tougher and is lobbying the Senate hard to come up with a more rigorous bill of its own. He even wants to go further than President Barack Obama in clamping down on current practices, because, says Gensler, the banks' "interests are not necessarily aligned with the American public's interests."

Gensler's years at Treasury and Goldman Sachs—at age 30 he became one of the firm's youngest partners—make him a formidable Wall Street foe, says CFTC Commissioner Bart Chilton. During agency discussions about rules on how firms trade and account for their transactions, "We've had times when someone says, 'The banks tell us they can't do that,'" Chilton recounts. "And Gary says, 'That's crazy. I used to do it all the time.'"

Gensler's biggest beef these days is with the loopholes embedded in derivative legislation. Unregulated derivative trading contributed mightily to the financial crisis when it turned out many investors could not pay off the derivative contracts they had written. Appalled by the damage done by reckless trading, the House voted to require that derivative dealers settle their transactions through clearinghouses. Traders working through clearinghouses would pledge capital to insure against the risk of any member defaulting on a trade. The clearinghouses would also make it easier for the CFTC to monitor trading.

But the House bill allows many exemptions to the clearinghouse rule, especially for nonfinancial companies seeking to hedge against currency swings, fuel costs, and other ordinary risks. Gensler argues that even these innocent-seeming exemptions will give openings to hedge funds and other financial firms that take big risks on derivatives to juice profits. As a result, he has now raised hackles at many corporations beyond Wall Street—they see the clearinghouses as burdensome and costly. On Feb. 3, the Senate got a letter from 180 companies, including Caterpillar and Boeing, warning of dire consequences if Gensler gets his way.

BRENDAN SMIALOWSKI/GETTY IMAGES

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Gensler is not giving up. He petitions the Senate constantly on the need for strong regulation. To extend his influence, he offers himself as a tutor to legislators on how the markets function. He also helps lawmakers spot small details that make a big difference. While the House legislation on derivatives was being drafted last year, bank industry lobbyists pushed to keep the current system of reporting trades through electronic systems set up by the banks. Gensler told lawmakers that such "confirmation facilities" were less transparent than an open exchange would be. He got the language that preserved the status quo removed from the bill.

CHANGE OF HEART

Gensler's new role as a regulatory crusader contrasts sharply with his days as a Wall Street hotshot. A Baltimore native, he worked at Goldman from 1979 to 1997, mostly in mergers and acquisitions and then as chief of debt and currency trading in Japan. He shifted to government in 1997 and eventually worked under then-Treasury Secretary Lawrence Summers. He was on Summers' staff when President Bill Clinton signed the 2000 Commodity Futures Modernization Act. That legislation—which Gensler supported—exempted many derivatives from CFTC oversight. The law has been blamed for the rapid growth in credit-default swaps and other instruments that developed largely outside the purview of regulators—until many of the deals blew up.

The dangerous role derivatives played in the financial crisis helped change Gensler's views on regulation, although he says those views were evolving before the crisis. Still, when Obama tapped Gensler to run the CFTC, consumer groups worried he would not be an ally. Democratic lawmakers, suspicious of his background in the Clinton Administration and at Goldman, delayed his nomination for five months.

Activists aren't worrying now. "He's been the strongest advocate of reform" in the Administration, says Barbara Roper, director of investor protection for the Washington-based Consumer Federation of America. Former CFTC Chairman Brooksley Born, who had squared off against Gensler in the fight over deregulation, is pleasantly surprised. "He's committed to robust regulation," she says.

That doesn't mean he'll always get what he thinks is best. In the fight over the Senate bill, he may have to settle for partial wins, given the strength of his Wall Street opponents. With at least $15.5 million in stocks, bonds, and index funds (according to a 2008 financial disclosure form registered with the Office of Government Ethics), Gensler can take on the banks without fear of annoying potential employers. "I don't see myself going back to Wall Street," he says. "That's very liberating." |BW|

–With Tina Davis in Washington and Matthew Leising in New York

GARY GENSLER'S WISH LIST

How the chairman of the Commodity Futures Trading Commission would reshape the financial system:

NO EXEMPTIONS TO THE RULES

Gensler would toughen legislation passed by the House in December so that even derivatives traded by nonfinancial companies would go through clearinghouses.

ENCOURAGE MORE COMPETITION

The CFTC boss would like to break up the control that five big U.S. banks have over derivative trading by making all pricing information publicly available.

CURB THE EXTREMES IN OIL PRICES

Gensler wants to dampen speculation by limiting the energy futures that traders can buy. His push follows concerns in Congress that speculators helped drive oil prices to a record high in 2008.

BusinessWeek

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Judgment Day Care

Critters that can't experience the Rapture with their masters will be cared for on earth—for a fee

By Mike Di Paola

Many people in the U.S.—perhaps 20 million to 40 million—believe there will be a Second Coming in their lifetimes, followed by the Rapture. In this event, they say, the righteous will be spirited away to a better place while the godless remain on Earth. But what will become of all the pets?

Bart Centre, 61, a retired retail executive in New Hampshire, says many people are troubled by this question, and he wants to help. He started a service called Eternal Earth-Bound Pets USA that promises to rescue and care for animals left behind by the saved.

Promoted on the Web as "the next best thing to pet salvation in a Post Rapture World," the service has attracted more than 100 clients, who pay $110 for a 10-year contract ($15 for each additional pet.) If the Rapture happens in that time, the pets left behind will have homes—with atheists. Centre has set up a national network of godless humans to carry out the mission. "If you love your pets, I can't understand how you could not consider this," he says.





Centre's service promises to look after pets like Dixie after the Second Coming

Centre came up with the idea while working on his book, *The Atheist Camel Chronicles,* written under the pseudonym Dromedary Hump. In it, he says many unkind things about the devout and confesses that "I'm trying to figure out how to cash in on this hysteria to supplement my income."

Whatever motivates Centre, he has tapped into a source of genuine unease. Todd Strandberg, who founded a biblical prophecy Web site called raptureready.com that draws 250,000 unique visitors a month, agrees that Fido and Mittens are doomed. "Pets don't have souls, so they'll remain on Earth. I don't see how they can be taken with you," he says. "A lot of persons are concerned about their pets, but I don't know if they should necessarily trust atheists to take care of them."

This paradox poses a challenge for Centre. He must reassure the Rapture crowd that his pet rescuers are wicked enough to be left behind but good enough to take proper care of the abandoned pets. Rescuers must sign an affidavit to affirm their disbelief in God—and they must also clear a criminal background check. "We want people who have pets and are animal lovers," Centre says. They also must have the means to rescue and transport the animals in their charge. His network consists of 26 rescuers covering 22 states. "They take this very seriously," Centre says.

One of Centre's atheist recruits is Laura, a woman in her 30s who lives near the buckle of the Bible Belt in Oklahoma, and who prefers not to give her last name. She has two dogs of her own and has made a commitment to rescue four dogs and two cats when—if—the time comes. "If it happens, my first thought will be, 'I've got work to do,'" Laura says. "The first thing I'll do is find out where I need to go exactly."

The rescuers won't know the precise location of the animals until the Rapture arrives, at which time they will contact Centre for instructions. "I've got to get to [the pets] within a maximum of 18 to 24 hours. We really don't want them to wait more than a day." A day she believes will never come.

Centre doesn't think he will ever have to follow through on the service he offers. But he believes in virtuous acts. His Web site directs about $200 a month in proceeds from Google ads to food banks in Minnesota and New Hampshire. And to pet owners, he has already delivered something of great value: peace of mind, for just 92¢ a month. "If we thought the Rapture was really going to happen," Centre says, "obviously our rate structure would be much higher." BW

(TOP TO BOTTOM) BLOOMBERG; C. CENTRE/BLOOMBERG

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Burch's look has been described as retro cool with a modern twist

DONATO SARDELLA/WIREIMAGE/GETTY IMAGES

MANAGEMENT & LEADERSHIP

A Fashionista's Global Designs

Competitors thought Tory Burch was just another dilettante couturiere. Now she's rocking their world

By Cotten Timberlake

Women of means have long been lured to Madison Avenue by the high-priced boutiques of Prada, Hermès, and Chanel. Later this year, those synonyms for luxury will be joined by a brand selling decidedly more affordable clothes when Manhattan socialite Tory Burch brings her eponymous line to the neighborhood. A risky move? This is not her first time bucking the odds. "There were a lot of raised eyebrows when I started this company," says Burch. "Many thought it would be a vanity project."

Burch's success has stifled most accusations of dilettantism. People close to the privately held company say it will sell \$300 million worth of goods in 2010, about a third more than last year. To speed that growth, Burch has opened stores in Manila and Tokyo, and over the next three to five years she aims to open 100 more worldwide.

Burch, 43, studied art history at the University of Pennsylvania and spent the '90s doing marketing and public relations for Ralph Lauren and Vera Wang by day, and making the scene by night. Along the way she realized many big brands ignored stylish women unless they could pay \$1,000 for a handbag.

At the time, Burch was married to Christopher Burch, a financier who now runs J. Christopher Capital. (They are divorced, but he remains an investor.) He'd learned the rag trade by launching a preppy sportswear line called Eagle's Eye in the '70s, which he later sold, and believed his wife's observation could become a moneymaker. Shortly after Tory began experimenting with designs in their apartment, she received a visit from Robert Burke, then Bergdorf Goodman's fashion director. "There are few times when in 10 minutes you know something is going to be a big success," says Burke. "She'd thought it through, soup to nuts."

In February 2004, Burch opened her first store in Manhattan's Nolita district. On opening day her friends and their friends mobbed the place. Word spread through gossip and fashion magazines, and soon her signature tunic top caught the attention of Oprah Winfrey, who, of course, told America all about it. Today Burch has 25 namesake stores, and her clothes are sold in 450 other locations.

Neiman Marcus fashion director Ken Downing describes her look as retro cool with a modern twist, adding that she understands what regular women want; her \$450 handbags and \$195 sunglasses can be a revelation for those unprepared to pay twice as much for snootier labels. "That's what women are relating to," Burch says. "There's resistance to excess."

One customer adds a note of caution. "It's nice to have one or two pieces," says Jennifer Prentice, who sells medical equipment in Minneapolis. "But if you have a bunch, you scream 'Tory Burch,' because she does use that medallion logo a lot."

Burch's expansion plans are bold, but she says her company is debt-free, profitable, and generating enough cash flow to fuel her growth. People close to the company say the Burches and their investors last year sold a 20% stake to Tresalia Capital, a firm run by an heiress to Mexico's Corona beer fortune. "Every brand has ups and downs, and I am sure she will, too," says Peter E. Nordstrom, the merchandising chief at Nordstrom. "But her instincts are good." | BW |

"EVERY BRAND HAS UPS AND DOWNS, AND I AM SURE SHE WILL, TOO. BUT I THINK HER INSTINCTS ARE GOOD"

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The Gold-Plated Boardroom

Comp crisis? Not for big-time corporate directors. Their pay is soaring—in some cases, into the millions

By Nanette Byrnes

The Great Recession hasn't stopped the music inside America's boardrooms. According to compensation consultants Pearl Meyer & Partners, the typical director of a large corporation made $216,000 last year, up from $129,667 in 2003. For some, total compensation, including cash payments, stock grants, and other perks, has climbed above seven figures.

Directors can thank the Sarbanes-Oxley Act for companies' continuing largesse. SarbOx was created to protect

Edward A. Kangas

2008 board pay: $1,314,418 (Intuit, $374,888; Hovnanian Enterprises, $409,007; Tenet Healthcare, $404,046; United Technologies, $126,477)

■ Kangas, head of accountancy Deloitte Touche Tohmatsu from 1989 to 2000, joined Tenet when it was under scrutiny for Medicare billing irregularities and, he says, was "looking for a bit of a white knight."

John R. Huff

2008 board pay: $1,296,866 (BJ Services, $1,078,515; KBR, $218,351)

■ Huff, the chairman of oil and gas driller Oceaneering International, ran the company from 1986 to 2006. His work for oil services company BJ Services made up the lion's share of his director pay in 2008. Huff did not respond to a request for comment.

William K. Reilly

2008 board pay: $1,524,819 (Energy Future Holdings, $850,000; ConocoPhillips, $464,205; DuPont, $210,614)

■ The former EPA administrator under President George H.W. Bush, Reilly says he has helped DuPont clean up its Superfund liabilities, reduce its greenhouse gas emissions by 70%, and save $3 billion in energy costs.

Jack P. Randall

2008 board pay: $1,561,220 (XTO Energy)

■ An oil-and-gas investment banker, Randall has sat on the XTO board since 1997, and his firm, Jefferies & Co., does consulting and banking work for XTO. Both XTO, which is in the process of being acquired by Exxon, and Randall declined to comment. Much of his pay has been in XTO stock.

Milton Carroll

2008 board pay: $1,204,310 (CenterPoint Energy, $1,045,946; Halliburton, $158,364)

■ Carroll serves as chairman of CenterPoint, which provides electricity and natural gas to more than 5 million customers in six states. He says he "work[s] closely with our CEO to assure that the company's strategic direction is consistent with the board's goals."



Data: Equilar, SEC filings, *Bloomberg BusinessWeek* *Excludes pay from companies for which a director is also paid for other services mentioned

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shareholders by reining in corporate executives; before, many boards had become little more than rubber stamps for everything from merger strategy to executive compensation—to disastrous effect in the cases of Enron, WorldCom, and Tyco (page 64). SarbOx and other regulatory efforts sought to protect shareholders by empowering directors and making them more accountable.

People can debate how much executives have been brought to heel since SarbOx, though in one important sense boardships have been fundamentally changed: Directors work a lot harder. A decade ago a typical director attended four board meetings a year and devoted about 100 hours a year to various board tasks, according to the National Association of Corporate Directors. These days directors spend an average of 225 hours a year on board duties, attending an average of six board meetings a year and convening at other times for committee meetings. Board service is "a job now," says Patrick McGurn, a corporate governance expert at New York-based consulting firm RiskMetrics Group. Directors of companies most affected by the financial crisis have logged 400-plus hours a year. In 2008, JPMorgan Chase's board upped its meetings from 9 to 18, while AIG's board met 19 times.

Below is a list of the most highly paid directors in 2008 at the largest 1,000 public companies in the U.S., based on Securities & Exchange Commission data compiled by Equilar, a Redwood Shores (Calif.)-based pay researcher. The figures include equity, which can include grants from earlier years.* | BW |

Andrew J. McKenna

2008 board pay: $1,281,760 (McDonald's, $990,001; AON, $291,759)

■ Stock grants from McDonald's, where he serves as non-executive chairman, vaulted McKenna onto the list. He wasn't available for comment, but McDonald's says his pay reflects his strong leadership.

Anthony P. Terracciano

2008 board pay: $4,789,993 (SLM, $4.8 million; Sovereign Bancorp, zero)

■ Terracciano, a former executive at Chase Manhattan and First Union, is making a second career out of his chairmanship of student loan giant SLM. He declined to comment, but SLM says he has twice taken voluntary pay cuts and pushed back stock grants.

Shirley Ann Jackson

2008 board pay: $1,346,648 (Public Service Enterprise Group, $213,110; NYSE Euronext, $225,016; Medtronic, $193,275; FedEx, $210,548; IBM, $229,699; Marathon Oil, $275,000)

■ Jackson's day job is president of Rensselaer Polytechnic Institute; she was paid $1.6 million in 2008, says the *Chronicle of Higher Education*. She was unavailable for comment.

Arthur C. Martinez

2008 board pay: $1,186,399 (IAC/InterActive, $259,062; International Flavors & Fragrances, $208,696; HSN, $192,260; PepsiCo, $327,521; Liz Claiborne, $198,860; American International Group, joined in 2009)

■ The former CEO of Sears serves as chairman of jewelry and gadget retailer HSN and joined AIG in May 2009. Martinez did not respond to requests for comment.

Larry C. Glasscock

2008 board pay: $1,356,540 (Wellpoint, $853,750; Zimmer Holdings, $244,926; Sprint Nextel, $257,864)

■ The onetime CEO of health insurer Wellpoint made more than $80 million during his last four years as chief, and now serves as chairman. Glasscock, who didn't respond to requests for comment, recently announced he would be stepping down from the board in March.



PHOTO-ILLUSTRATION BY JOHN UELAND, (L TO R) PHOTOGRAPHS BY BLOOMBERG (HUFF); ROLLCALLPIX/NEWSCOM (REILLY); BOYLE/BLOOMBERG (McKENNA); NAGLE/BLOOMBERG (TERRACCIANO); GRAYLOCK/AP (JACKSON); LAMPEN/REUTERS (MARTINEZ); WELLPOINT INC./AP (GLASSCOCK)

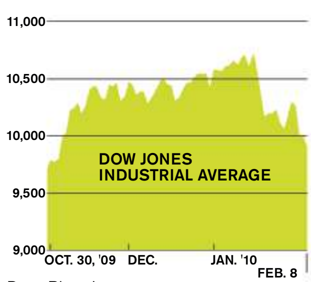
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75 Investing: Mutual funds that mastered the bear and bull markets
76 Life Management: Helping nonprofits raise money like Goldman

MONEY REPORT

FIBONACCI FORECAST: DOW DROPS 11%

An analysis, based on the golden ratio, says stocks peaked in January



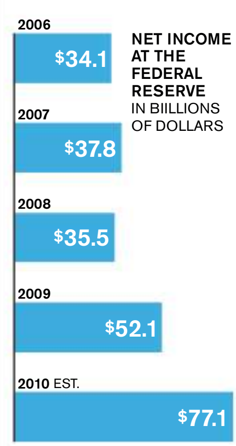
Data: Bloomberg

Want to divine where stocks are headed? Try using the golden ratio, the formula that has long influenced artists, architects, scientists, and mathematicians, including Leonardo Fibonacci in the 13th century. In stock analysis the number is said to reflect changes in investor sentiment and thus potential turning points in the market. Relying on the ancient math, Rick Bensignor, chief market strategist for brokerage Execution LLC, claims the Dow peaked at 10,725 on Jan. 19. He came up with the prediction by multiplying the benchmark's low of 6627 on Mar. 6, 2009, by 1.618, the golden ratio. Now, he thinks the Dow may drop at least 11% from that high, to 9545 or lower. The golden ratio isn't a perfect science. If investors had applied the same methodology to the trough of the Nasdaq or the S&P 500 in March, it would have underestimated the rally by a few percentage points, says Bensignor. *–Lu Wang*

FED WATCH

PSST! LOOKING FOR HOT TRADING TIPS? ASK UNCLE SAM

The Federal Reserve may have some investing tips for Wall Street. The Fed, which mainly makes money off its portfolio of Treasuries and other securities, is set to earn $77.1 billion in net income this year, according to the budget President Barack Obama just presented to Congress. As a group, the six largest banks—Bank of America, JPMorgan Chase, Citigroup, Wells Fargo, Goldman Sachs, and Morgan Stanley—are expected to earn only $55.3 billion. ***–Brendan Moynihan and Alex Tanzi***



Data: Federal Reserve, Office of Management & Budget

BANKS

WELLS FARGO BRACES FOR RISING RATES

Banks have been making fat profits by borrowing money at rates near zero and investing it in higher-yielding bonds. But Wells Fargo is sacrificing some short-term gains to protect itself against rising interest rates. The bank cut its bond holdings by $34 billion in the second half of 2009, giving up $1 billion in profits, according to figures in the company's filings. Rivals Bank of America, Citigroup, and JPMorgan Chase all added to their fixed-income portfolios in the same period.

Wells' strategy could pay off if rates climb higher or faster than expected; rising rates cut the value of existing bonds. "The bias is for higher rates," said Wells CEO John Stumpf in a conference call. "We're willing to wait for that to happen." He may have to wait a while. The Federal Reserve recently said it plans to keep rates low for "an extended period." *–Dakin Campbell*



Stumpf: The bank has cut its bond holdings

PHOTOGRAPH BY PATSY LYNCH/RETINA; (TOP TO BOTTOM) CHARTS BY ALBERTO MENA/BW; DAVID RUDES/BW

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INVESTING

MUTUAL FUNDS

FUNDS THAT RODE THE BEAR AND BULL

By Tara Kalwarski

Only 28% of mutual funds eked out cumulative gains over the two years ended Dec. 31, 2009, a period when the Standard & Poor's 500-stock index lost more than 20%, or about 11% per year. Here are the top 10 funds, with a look at how they succeeded—good timing and plenty of cash on hand helped.

FUND	NAME/TICKER	ANNUALIZED	TOTAL RETURN 2008	TOTAL RETURN 2009
Specialty	Robeco BP Long/Short Equity BPLEX	19.3%	−21%	81%
Specialty	Delaware Healthcare DLHAX	18.6	−13	61
Bond	Old Mutual Dwight High Yield ODHYX	16.1	−16	60
Stock	Reynolds Blue Chip Growth RBCGX	16.0	−5	42
Bond	MainStay 130/30 High Yield MYHAX	14.6	−15	54
Stock	Appleseed APPLX	14.5	−18	60
Bond	Dreyfus International Bond DIBAX	14.2	11	17
Stock	Intrepid Small Cap ICMAX	14.0	−7	40
Stock	Forester Discovery INTLX	13.0	8	19
Stock	Catalyst Value CTVAX	12.8	−24	67

Data: Morningstar

STOCK FUNDS

At one point in 2008, **Reynolds Blue Chip Growth** was 98% in cash. The fund lost 5% for the year. Manager Fritz Reynolds says he began deploying that cash near the market bottom in early 2009. Now, about a third of the fund is in blue chips like Caterpillar and Deere that should profit from a global recovery. **Forester Discovery**'s Tom Forester limits his downside by "buying good international value stocks" like Petrobras and keeping cash on hand—it's 40% of the fund: "We're cautious right now."

BOND FUNDS

Dreyfus International Bond expected a rough 2008, so manager Dave Leduc sold riskier debt to get into safer government-backed securities in the U.S., Germany, and France. Since late 2008 the fund has added emerging-market debt and bought high-quality bonds of companies like Coca-Cola and IBM. **MainStay 130/30 High Yield** gets top marks for risk-adjusted returns. The fund uses a hedging strategy and is fully invested in high-yield bonds, including ones from Ford and GM, that it bought cheap.

SPECIALTY FUNDS

Over the past decade buying cheap stocks and shorting overvalued ones led **Robeco BP Long/Short Equity** to an average annual return of 15%. **Delaware Healthcare** manager Liu-Er Chen, who ran a health-care fund at Evergreen Investments before moving to Delaware Investments in 2006, says that the acquisitions of holdings Barr Pharmaceuticals and Genentech helped rank them among the top contributors to fund performance. He says he favors defensive blue-chip stocks, like Pfizer and Eli Lilly, now more than ever before.

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SECOND ACTS

BANKING ON A GOOD CAUSE

By Amy Feldman

As an investment banker at Goldman Sachs, Charles "Chuck" Harris helped raise billions of dollars for companies. Now the retired partner, 58, is happy if he raises mere millions. The funds don't fatten company coffers, though. They help improve education for low-income kids, an issue he cares about deeply.

Four years ago, Harris founded New York-based SeaChange Capital Partners with another ex-Goldman partner, Robert Steel, to bring Wall Street capital-raising methods to the nonprofit world. His idea is that nonprofits are held back by the time and effort it takes to raise funds in dribs and drabs for one project or another. By raising larger sums of money at one point in time—similar to the way a company would with venture capital or an initial public offering—nonprofit managers can stop worrying about cash and start focusing on their programs. "Imagine trying to grow a company with no financial certainty," he says. "Companies do not do that, and, it seems to me, well-managed nonprofits shouldn't either."

Before Harris hit on that idea, he had quit Goldman twice. The first time was in 1996, at age 45, to spend more time skiing, golfing, and with his family. He rejoined in 1999, when he was offered a job working part-time near his Connecticut home with the firm's technology investment banking group. He left for good in late 2002, after the tech bubble burst. "It was all part of a journey to find what work to do next," he says. "I had a great experience working there. It was a job, if you will, not a passion. But because we did well at Goldman, it allowed me the flexibility to find my passion."

The second time Harris left Goldman, he did so to chair a major capital-raising campaign for his alma mater, Phillips Exeter Academy. (The campaign raised $350 million.) Harris, who was a scholarship student at Exeter, says going to the elite prep school changed his life. Gradually, Harris got more involved in fund-raising and joining boards of directors. In two test cases of what would become SeaChange's model, Harris helped raise tens of millions for College Summit, which tries to improve enrollment rates, and Teach for America, which recruits college grads to teach in public schools.

Harris helps nonprofit education organizations raise big money

With those two pilots completed, SeaChange—which got funding from Goldman, the Gates and Hewlett foundations, and others—set out to create a network of donors willing to make multiyear, six-figure commitments. At the same time, SeaChange started scouting for education-focused organizations on the point of expansion.

The first two nonprofits that SeaChange is working with, out of more than 100 it considered, are Uncommon Schools, which runs charter schools in Brooklyn, N.Y., and Newark, N.J., and New Teacher Center, which trains educators to work in inner-city schools. For New Teacher Center, the goal is $3 million. For Uncommon Schools, SeaChange's original goal was $30 million. But with the economy slow and would-be donors strapped, so far only $6.3 million has been committed and Harris has scaled back his hopes to $15 million. That campaign ends in May. "We are engaged in day-to-day combat to get there," Harris says. "You can't tell a program that's trying to grow to raise money along the way. They need the money now." | BW |

FAMILY
Wife, Susan, is an artist and fabric designer. They have twin sons.

MENTORING
Co-hosted a gathering of Exeter alums through Civic Ventures, an organization devoted to helping people find meaningful second careers.

GIVING
Seeded SeaChange with $500,000 from personal funds.

JENNIFER S. ALTMAN

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80 Tech & You: Palm's Mobile Hotspot
81 Feedback
84 Outside Shot: The power of straight talk

BUSINESS VIEWS



BOOKS By CATHERINE ARNST

Make a List. Check It Twice

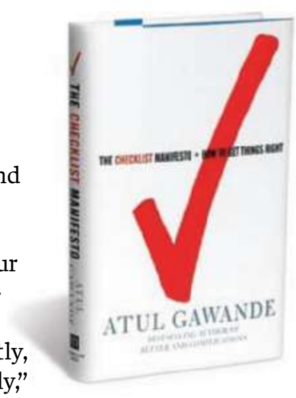
How tragic errors can be sharply reduced with a piece of paper, hand-drawn boxes, and a pencil

Dr. Atul Gawande, a surgeon and *New Yorker* writer, had a huge impact on the health-care reform debate last summer when he wrote about wide regional disparities in Medicare spending. The article focused on McAllen, Tex., one of the country's priciest health-care markets. Gawande's conclusion—that doctors in McAllen charge more not because their patients are sicker or their care is better but simply because they can—caught the attention of reform forces across the nation. President Barack Obama had his entire staff read it.

Gawande may end up wielding influence again with his new book *The Checklist Manifesto: How to Get Things Right*. He starts the book by explaining how a simple five-item checklist in the operating room can dramatically reduce hospital-acquired infections, which kill 99,000 Americans a year.

But the scope of the book goes well beyond medicine. With *The Checklist Manifesto*, Gawande has entered Gladwell-land. Fellow *New Yorker* writer Malcolm Gladwell has produced three best sellers—*The Tipping Point, Blink,* and *Outliers*—by stacking up detailed, seemingly unrelated anecdotes to bolster a larger, universal thesis. Gawande follows the same blueprint, examining all manner of disparate tasks, from flying a plane to building a skyscraper, to show how checklists can improve outcomes. Read this book and you might find yourself making checklists for the most mundane tasks—and be better off for it.

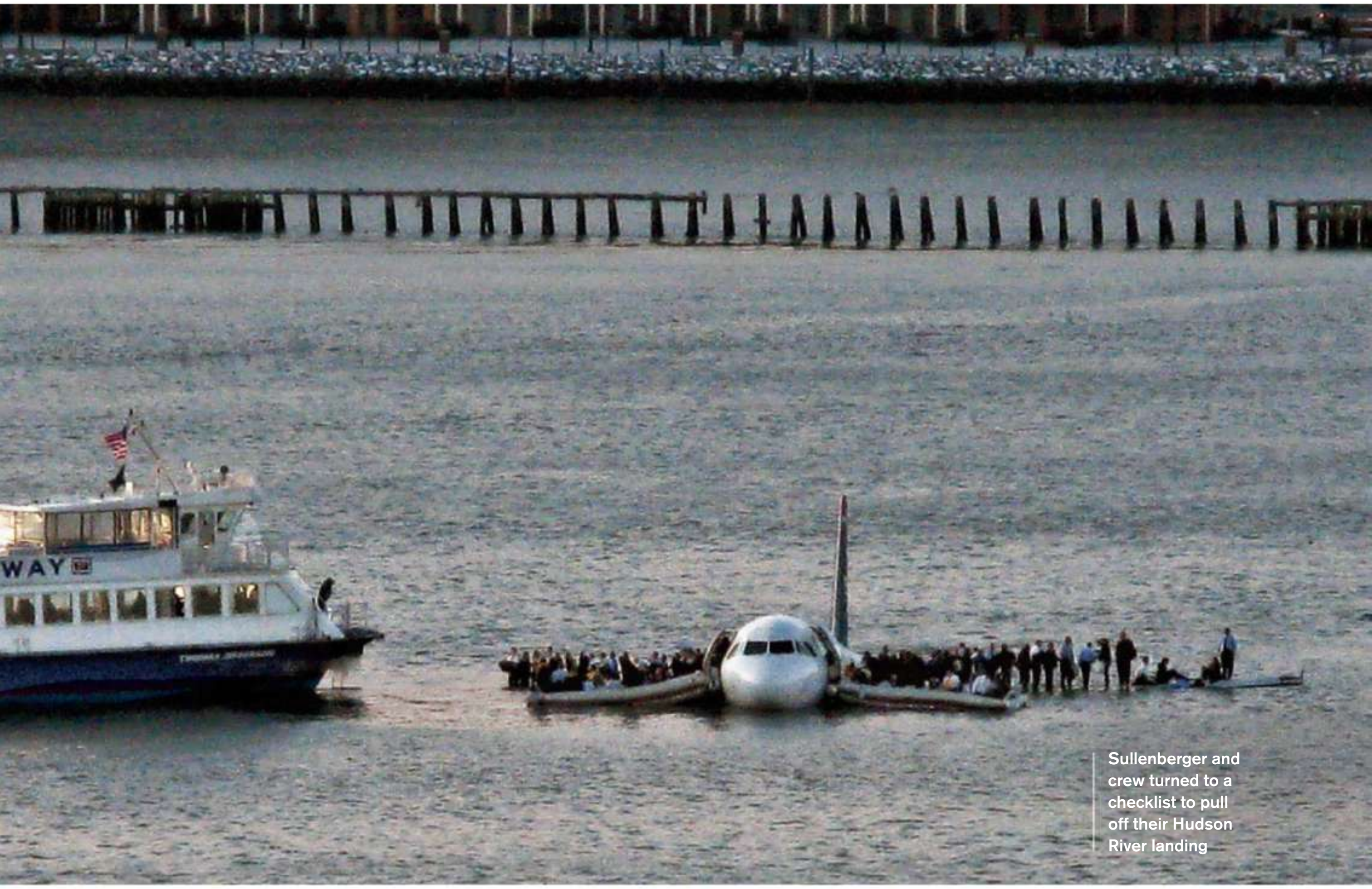
Gawande tells scarifying stories about the things that go wrong in operating rooms. Despite all the training and high-tech tools, doctors can forget the most basic steps, and chaos ensues. That's just as true in a range of other fields, from finance to government. "The volume and complexity of what we know has exceeded our individual ability to deliver its benefits correctly, safely, or reliably," writes Gawande. Unless, of course, we use checklists.



The Checklist Manifesto: How to Get Things Right
by Atul Gawande
Metropolitan Books; 209 pp; $24.50

Gawande proves his point through a steady accretion of examples, starting with the Boeing B-17. In 1935 the bomber crashed on its first test flight because it proved too complex for the skilled test pilot to manage. The U.S. Army Air Corp ordered planes from Douglas instead, and Boeing

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Sullenberger and crew turned to a checklist to pull off their Hudson River landing

STEVEN DAY/AP PHOTO

nearly went bankrupt. But some test pilots believed in the B-17. They came up with a takeoff checklist to guide a pilot through all the crucial steps to get the plane airborne. Checklists in hand, pilots went on to fly the B-17 for more than 1.8 million miles without an accident. The army ultimately ordered 13,000 B-17s, giving the U.S. a decisive air advantage in World War II. And pilot checklists became universal.

Dr. Peter Pronovost, a critical care specialist at Johns Hopkins, devised his own operating room checklist in 2001. On a plain sheet of paper he wrote out five steps doctors and nurses in the OR should follow, all "no-brainers," as Gawande puts it: Wash your hands with soap, sterilize the patient's skin, put sterile drapes over the entire patient, wear a mask, gown, and gloves, and put a sterile dressing over incisions. Within a year the rate of infections related to IV tubes at the hospital went from 11% to zero. Only two such infections occurred over the next 15 months. Michigan instituted Pronovost's five steps in every hospital in the state, and within three months infections related to IV tube insertions dropped 66%.

It's not always so easy. Gawande tells of his own efforts to set up a similar but expanded checklist at his hospital, Brigham & Women's in Boston. Turns out his first effort was far too complex and had to be abandoned within hours. It took many more tries, and lots of research, to get it right.

Once you nail them, however, checklists can create heroes, Gawande claims. For proof he gives us US Airways Flight 1549, which famously landed on the Hudson River in January 2009 after hitting a flock of geese near New York's LaGuardia airport. Captain Chesley B. Sullenberger III has been hailed worldwide for the seemingly miraculous landing. But Gawande shows that Sullenberger and his co-pilot followed a detailed emergency checklist that multiplied his chances of pulling it off. The experienced crew recognized that it required teamwork, preparation, and discipline to bring the plane down safely. "This is what it means to be a hero in the modern era," says Gawande. BW

Checklist for the Perfect Checklist

To make complex operations routine, keep these guidelines in mind:

- ☐ Include all "stupid but critical" tasks so they're not overlooked
- ☐ Make it mandatory for team members to let others know when they complete one of those tasks
- ☐ Empower subordinates to question their superiors about the checklist
- ☐ Allow for improvisation in unusual circumstances
- ☐ Thoroughly test-drive your checklist before putting it into practice

Data: *Checklist Manifesto*

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TECH & YOU

By RICH JAROSLOVSKY

Welcome to My Mobile Hot Spot

Palm's new smartphone lets friends and family into your private Wi-Fi circle

No two ways about it: I am one hot guy. Not *that* way, though don't I wish. I'm generating heat because I'm carrying Palm's new Pre Plus smartphone, which turns me into a walking, talking Wi-Fi hot spot; wherever I go, I can allow lesser mortals to share my phone's Internet connection. It's like having a superpower I choose to share for the good of the world.

The original Pre, which debuted last year on Sprint Nextel's network in the U.S., featured a striking "smooth stone" design and an elegant operating system called webOS. Better yet, it didn't scream "iPhone wannabe"—unlike, say, Google's Nexus One. The Pre's one big drawback was its limited number of apps. The Pre Plus, now available on the much larger Verizon Wireless network, doesn't solve the app problem—and it costs a hefty $150 on a two-year contract after a $100 mail-in rebate. But the new Mobile HotSpot application very nearly makes up for these drawbacks.

The Pre Plus, while compact, is still chunkier than Apple's iPhone or the Nexus One, which is manufactured by HTC. In repose, the screen is all shiny blackness, since the function button has been replaced by a slender stripe across the bottom that is only visible when the screen is in use. Sliding the screen up reveals a tiny physical keyboard. Too tiny, in fact; if you're a thick-fingered typist like me, you'll keep hitting the wrong keys. My best advice is to try using the edge of your fingernail.



Palm's Pre Plus lets up to five devices share its signal

The app situation has improved somewhat. The number of programs has inched up to about 1,000—or 139,000 fewer than the number available for the iPhone and 19,000 fewer than those for Google's Android operating system, which drives the Nexus One and Motorola's Droid. But with apps for Facebook and Twitter, plus games, including Need for Speed Undercover and The Sims 3, your hands will never be idle.

The real fun begins with Mobile HotSpot. It lets up to five Wi-Fi-capable devices share the Internet connection of a Pre Plus or $100 Pixi Plus, the Pre's lightweight sibling. Once you install it and establish a password, you will pop up on other people's Wi-Fi-equipped phones and laptops as a "webOS network." Anyone entering your password is then able to make use of the phone's 3G connection. You can imagine the advantages. In a carpool or on a family trip, passengers can all do their own thing. You're freed from the tether of Starbucks or other commercial Wi-Fi locations; any public space where you can get a 3G signal from Verizon becomes a hot spot.

The signal range is impressive. Placing the Pre Plus on a colleague's desk, I was still able to surf the Web on a laptop about 200 feet away. Speed was variable but I found it more than acceptable even with multiple devices attached.

Drawbacks? Price is one. Verizon charges $40 a month for up to five gigabytes of data. That's less than what it charges to use Novatel Wireless's MiFi, a standalone device that provides the same capability. But coming on top of your regular data plan, it's not a trivial expense. There's also a toll on your battery; the Mobile HotSpot app sucks power like a thirsty teenager slurps a soft drink. With two devices connected in addition to the phone itself, I plowed through most of a fully charged battery in about three hours. If you're using the feature for more than a quick Internet session, you'd better be near an outlet or a car cigarette lighter.

But what difference does all that make compared with the sense of power you get from controlling other people's online access? If I like you, it's my world and welcome to it. If I don't, it's hey, you—get off of my cloud. |BW|

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FEEDBACK

AT&T

RATING AT&T, FROM INSIDE AND OUT

"AT&T's iMess" (In Depth, Feb. 15) went out of its way to ignore the facts. Yes, the smartphone phenomenon has created demand for network capacity that exceeded everyone's estimates. What has resulted is AT&T leading the world in mobile broadband, supporting two times more traffic than any other company around.

The reporter relied heavily on the comments of an analyst at a firm that does not regularly follow AT&T or telecommunications but chose to ignore or not seek the perspectives of the 18 financial analysts who have a buy rating on AT&T.

Amazingly, the story questions our capital spending in recent years without noting that AT&T invested more than any other U.S. telecom or cable company last year and more than any U.S. company in 2008. As a result of those investments, our 3G network can support twice as many smartphone users as any of our peers.

AT&T provided vast amounts of information, resources, and references for this piece. Virtually all of it was ignored.

Cathy Coughlin
Senior Executive Vice-President and Global Marketing Officer
AT&T
DALLAS



I take strenuous issue with the apologists and shills for AT&T. I'm neither. I'm just a business owner. We recently bought our way out of the remaining 13 months on our AT&T contract because AT&T, in my view, is selling and collecting for a service that it cannot deliver. The assertion that complaints are generally isolated to a few areas of high user density (Manhattan, Los Angeles, etc.) is just 100% bogus. We live in a town of 7,000. Until we ditched AT&T three months ago, being able to make a call was the exception, not the rule.

Screen name: Warren Miller

HEALTH CARE

READING A PAMPHLET ISN'T EXERCISE

Disease management misses the mark ("Take Your Meds, Exercise—and Spend Billions," In Depth, Feb. 15). Phone calls from nurses, newsletters, and online charting of symptoms is like watching an exercise show on TV and expecting results. Companies need to do simple things, like install bike racks or issue routes with mileage for walking during the lunch hour. Tangible, concrete actions trump all the slick health information sent by disease management companies.

Screen name: Mark Siepker

TAXES

THE TAX BURDEN OBAMA OVERLOOKS

Regarding "Taxes: Ready to Rumble" (Special Report, Feb. 1): President Barack Obama and his advisers really don't get it. Just as all companies are ultimately owned by individuals, all corporate taxes are ultimately paid by individuals. But corporate taxes are far worse than just a costly, opaque way to collect individual taxes. Given that taxes are a major factor in choosing to locate operations, corporate taxes only provide incentives to move jobs elsewhere.

Chris Waldorf
SEATTLE

HAITI

'BUSINESS AS A SOLUTION TO POVERTY'

Bill Clinton is right to note how business investment can change the situation in Haiti ("Business Can Help Haiti," Business Views, Feb. 15). I see a new trend in aid efforts that use business as a solution to poverty. For example, Tifie Humanitarian seeks business opportunities in countries investors shun. Its agriculture trucking business in the Democratic Republic of Congo bought big trucks and drove to villages to gather goods that could not reach the city. All profits from these goods go to the villages, and all revenue stays in the country.

Screen name: David Griffith

DARRELL ISSA

KEEP THE HEAT ON TIM GEITHNER

My congressman, Darrell Issa (R-Calif.), is right to go after Tim Geithner and Ben Bernanke on AIG ("Geithner's Tormentor," New Business, Feb. 15). They're not telling us the whole truth about AIG.

William Thayer
SAN DIEGO

CORRECTIONS & CLARIFICATIONS
The "At the Table" interview of NBA Commissioner David Stern (Feb. 15) contained a transcription error: It should have said the audience for NBA TV is approaching 50 million homes, not 15 million.

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COMPANY INDEX

The index lists significant references to companies, top executives, public officials, and well-known figures around the globe. The folio denotes the first page of the story containing the reference.

A Actis Capital 30
Adobe (ADBE) 24
Aetna (AET) 29
AIG (AIG) 72, 81
Amazon.com (AMZN) 24
AmerisourceBergen 64
Anglo Irish Bank 50
Apple (AAPL) 24, 66, 80
AT&T (T) 24, 81
Autodata 38
Automatic Data Processing (ADP) 16
AutoStratagem 38
B Banco Uno 46
Bank of America (BAC) 68, 74
Bank of New York Mellon (BK) 68
Barrett, Craig R. 50
Barr Pharmaceuticals 75
Batista, Eike 14
Becker Capital Management 66
Bergdorf Goodman 71
Berkshire Hathaway (BRK.A) 74
Bernanke, Ben 8
BlackRock (BLK) 67
Blackstone (BX) 8
Blankfein, Lloyd 32
BlueGold Capital Management 18
Boeing (BA) 38, 68, 78
Born, Brooksley 68
BrainReserve 38
Breen, Edward D. 64
Broadview Security (CFL) 64
Brown, Scott 29
Burch, Tory 71
C **Capellas, Michael** 46
CardServices International 46
Careline International 50
Carey, Kevin 50
Cargill 68
Carlyle Group 30
Caterpillar (CAT) 75
Chanel 71
Charles River Associates (CRAI) 67
China Investment 8
Chrysler 32, 38
CIT Group (CIT) 8
Citigroup (C) 68, 74
Clinton, Bill 68
Coca-Cola (KO) 8, 75
CommScope (CTV) 64
Community Health Systems (CYH) 29
Cote, David 32
Cowen & Co. 22
Credit Suisse (CS) 26, 68
Crossover Technologies 66
D Decision Economics 16
Deere (DE) 75
Delaware Healthcare 75
Delaware Investments 75
Dell (DELL) 50
Deutsche Bank (DB) 30, 68
Deutsch LA 38
Dimon, Jamie 32
Doerr, John 32
Domino's Pizza (DPZ) 84
Doyle, J. Patrick 84
Drendel, Frank M. 64
Dreyfus International Bond (DIBRX) 75
Dunkelberg, William 16
E East West Hospitality 30
Edmunds.com 38
Eli Lilly (LLY) 75
eMarketer 22
Equilar 72
Eternal Earth-Bound Pets USA 70
Evergreen Investments 75
Execution LLC 74
F Facebook 8, 66
FBR Capital Markets (FBCM) 64
FedEx (FDX) 32
Fiat (FIATY) 38
First Data 46
Ford (F) 32, 38, 75
Forester Discovery (INTLX) 75
FriendFinder Networks 46
Fuld, Dick 8
G GameStop (GME) 66
Gawande, Atul 78
Geithner, Tim 32
Genentech (DNA) 75
General Electric (GE) 32, 64
General Motors 32, 38, 75, 84
Gensler, Gary 68
Gladwell, Malcolm 78
Goldman Sachs (GS) 54, 68, 74, 76
Google (GOOG) 8, 22, 24, 80
Grübel, Oswald J. 26
Guinness 50
H Hair Club 22
Harris, Charles "Chuck" 76
Health Management Associates (HMA) 29
Health Net 29
Hedge Fund Research 67
Hellenic Telecommunications Organization 18
Hermès 71
High Frequency Economics 16
Honda (HMC) 38
Honeywell (HON) 32
HTC 80
Hyatt (H) 22
Hyundai 38
I IBM (IBM) 75
IHS Global Insight 38
Immelt, Jeff 32
Innolux 24
Integrated Media Solutions 22
Intel (INTC) 50
iSuppli 24
J J.D. Power Associates (MHP) 38
Jetpay Merchant Services 46
Jobs, Steve 24
Jollibee 30
JPMorgan Chase (JPM) 68, 72, 74
K Kia Motors 38
Kleiner Perkins Caulfield & Byers 32
Kohlberg Kravis Roberts (KFN) 46
Kozlowski, Dennis 64
L Lehman Brothers 8, 32
LG Display (LPL) 24
LifePoint (LPNT) 29
Lutz, Robert 38
M MainStay 130/30 High-Yield (MYHAX) 75
MasterCard Worldwide (MA) 46
Mazda 38
McCann Erickson 38
McDonald's (MCD) 8, 30
Merrill Lynch (MER) 8
Microsoft (MSFT) 38
Morgan Stanley (MS) 8, 68, 74
Motorola (MOT) 64, 80
MTS Health Partners 29
Mulally, Alan 38
N Neiman Marcus 71
Nissan 38
Novak, David C. 30
Novatel Wirless (NVTL) 80
O **Obama, Barack** 29, 32
Offshore Merchants 46
Optimal Payments 46
Oyster European Opportunities Fund 26
P Palm (PALM) 80
Papandreou, George 18
Paycom 46
Payment Resource International 46
PayNet 16
Pearl Meyer & Partners 72
Penguin 24
Penthouse Media Group 46
Petrobras (PBR) 14, 75
Pfizer (PFE) 75
Piper Jaffray (PJC) 24
Playfish 66
Prada 71
R Ralph Lauren 71
Rasmussen, Poul 67
Republic Bank 46
Reynolds Blue Chip Growth (RBCGX) 75
RiskMetrics Group 72
Robeco BP Long/Short Equity 75
Royal Bank of Scotland (RBS) 50
S Samsung 24
Sanford C. Bernstein (AB) 64
SAP (SAP) 8
SeaChange Capital Partners 76
Seidenberg, Ivan 32
Shepherdson, Ian 16
Simon & Schuster 24
Smith, Fred 32
Sony (SNE) 24
Sprint Nextel (S) 80
Starbucks (SBUX) 80
Sterling Market Intelligence 22
Strategic Visions 38
Stumpf, John 74
Sullenberger III, Chesley B. 78
Summers, Larry 32, 68
T Take-Two Interactive (TTWO) 66
Thain, John 8
Toyota (TM) 8, 32, 38
Tresalia Capital 71
Twitter 8
Tyco (TYC) 64, 72
U UBS (UBS) 26, 46
UnitedHealth (UNH) 29
United Technologies (UTX) 64
UPS (UPS) 32
US Airways (LCC) 78
V Vale (VALE) 14
Vera Wang 71
Verizon (VZ) 32
Visa (V) 46
Vontobel Holding 26
Vourloumis, Panagis A. 18
W Waterford Wedgwood 50
Wedbush Morgan Securities 66
WellPoint (WLP) 29
Wells Fargo (WFC) 74
Whitacre, Edward Jr. 38
Y **Yost, David** 64
Yum! Brands (YUM) 30

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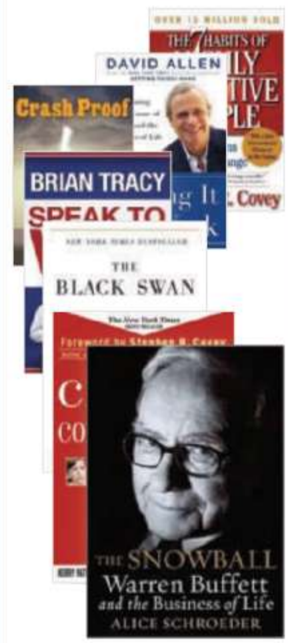
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OUTSIDE SHOT

By PATRICK LENCIONI

The Power of Saying 'We Blew It'

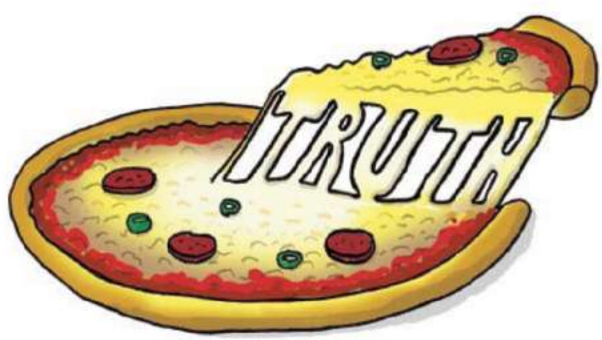
New ads for Domino's Pizza display unusual corporate vulnerability—and the surprising effectiveness of talking straight

I recently saw a television commercial that made quite an impression on me, and I have a hunch that it might go down as one of the most effective advertisements of all time, assuming the company behind it is sincere. I'm talking about Domino's Pizza and the recent ad in which the company concedes the shortcomings of its product and explains what has been done to improve it.

The spot opens with customers describing Domino's pizza using words like ketchup and cardboard. Then, Domino's President J. Patrick Doyle matter-of-factly explains the importance of acknowledging how customers see his pizza. Finally he outlines the company's response: 40% more herbs in its sauce, better cheese, a special glaze on the crust. I have a hard time remembering the names of the U.S. Supreme Court justices and even what I had for breakfast. But I can remember all those details from the Domino's ad, and that says a lot about its impact.

I'm willing to bet that Domino's will sell a lot more pizzas in the months ahead. And the reason I believe that has less to do with the new ingredients than with Domino's willingness to cross a line that most companies—and for that matter, most leaders—won't even approach. Domino's chose to make itself vulnerable.

Vulnerability isn't a word that shows up on lists of ingredients for business success. Here's why it should: Without the willingness and ability to be vulnerable, we simply can't build deep and lasting relationships in business and, come to think of it, life.



Vulnerability is often seen as a weakness; it's actually a sign of strength. People who are genuinely open and transparent prove that they have the confidence and self-esteem to allow others to see them as they really are, warts and all. There's something undeniably magnetic about people who can do that.

When it comes to the workplace, vulnerability is critical in the building of teams. When teammates feel free to admit their mistakes, ask for help, and acknowledge their own weaknesses, they reduce divisive politics and build a bond of trust more valuable than almost any strategic advantage. Another great venue for vulnerability is the one I work in, the world of service. When consultants and advisers are willing to ask dumb questions, tell the unvarnished truth, or broach the painful, elephant-in-the-room topic, they engender loyalty and trust with clients.

Getting back to Domino's, I think the most fascinating application of vulnerability is in marketing and advertising. It's so rare that it packs a strong punch, as long as companies mean it. Go ahead and try to think of other corporate examples of humility and naked honesty. There aren't many to choose from.

One is General Motors, which emerged from bankruptcy last summer offering this slogan: "General Motors needs to start over in order to get stronger." More recently, the Chicago Bears capped off a miserable season by buying a full-page ad admitting to a subpar attempt at professional football and thanking fans for their support in spite of the team's mediocrity.

But the Domino's ad struck me as particularly potent, perhaps because it doesn't spring from a crisis at the company (its market share has been holding steady). You wouldn't be wrong to call it countercultural, though I hope that will change. As consumers, we are so used to companies exaggerating and embellishing that we've learned to be skeptical, even cynical.

That's why Domino's made me do a double take. And I know there are a lot of people out there like me who will give a second chance—or even a first one—to a company that shows that kind of courage. | BW |

Patrick Lencioni is the author of a new book, Getting Naked, *and the best seller* The Five Dysfunctions of a Team. *He is founder and president of management consultancy The Table Group.*

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